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### **Defining Accountability**

Accountability of a government to citizens is one of the valuable dimensions holding together democratic societies. Public accountability underpins the governance of civilized communities, and is the lifeblood in guarding the public interest. Governments have the ultimate power in making decisions when balancing the interests of various sectional and business groups, but the price for this through the history of western liberal democracies has been a suitable system of accountability to guard such power. Whether simply through the polls, or else through a longer and more complex chain of responsibility for decisions and actions, accountability is at the heart of the modern democratic state. Symbolically, it conveys an image of transparency and trustworthiness, and is “one of those golden concepts that no one can be against”; Bovens et al (2008). It is a central notion in the rhetoric of ‘good governance’, when seen as democratic political processes along with accountable systems of government. Technically, though, it is also, as Barberis (1998) put it, “an old and tricky subject”, as well as being a “slippery, ambiguous term” (Day & Klein 1987).

The underpinning idea of accountability is simple enough. When we are requested by others to achieve something, we report back to them on how we have performed (Hughes 2003:237). In other words, it is answering for one’s actions (Ott & Russell 2001). Accountability may be more than simply answering questions, too, and involve ‘setting goals, providing and reporting on results and the visible consequences for getting things right or wrong, including rewards or sanctions as appropriate’ (Funnel & Cooper 1998:30).

More formally, Mulgan (2003:1) defines accountability as “the obligation to be called to account”. Or in the alternative words of Day and Klein (1987), accountability means the responsibility of one party, the accountability holdee, to justify its actions to another, the accountability holder, according to a pre-existing set of rules, standards or expectations. It is “the right of the account-holder to investigate and scrutinize the actions of the agent by seeking information and explanations and the right to impose remedies and sanctions” (Mulgan 2003:10). It has, though, been broadened to include the role of responsibility, the expectation to control (as distinct to simply giving an account after the event), and the desire to encourage responsiveness. Under this broader meaning, accountability is nowadays firmly connected to notions of assessment, blame, redress, explaining and changing behaviour after failure (Mulgan 2003), as well as transparency, control, responsiveness and improving performance.

Accountability is thus about “giving account”, as Mulgan says. Bovens et al (2008) go even further than this, noting that the forum in which account is given along with the possibility that sanctions may be applied also matter. To them, accountability is a “relationship between an actor and a forum, in which the actor has an obligation to explain and justify his or her conduct, the forum can pose questions and pass judgment, and the actor may face consequences”.

Of course, the notion of accountability operates at many levels within a society; government (or political accountability), institutional (corporate accountability), project or team (management accountability) or individual (personal accountability). Such notions also have relevance across all three sectors; public, private and not-for-profit. At the highest level of governance, democratic political systems aspire, in the words of

Abraham Lincoln's 1863 Gettysburg Address, to an ideal of "government of the people, by the people, for the people". At the institutional level, governance embodies a range of disciplines on directors and managers as well as some expectation of working as a good corporate citizen. And at the personal level, planning and then measuring our personal achievements is a useful practice. Whilst this article will cover a range of areas of accountability, our discussion will emphasize accountability principles as they relate to public matters.

## History

The history of accountability in the public sphere parallels the history of public administration. Farazmand (1998) tells us that Iran (or Persia) has had 8,000 years of tradition in bureaucracy and public administration on a massive scale. They were the first people to adopt the concept of 'the state' and forged a world-state empire, through a trained, professional bureaucracy based on merit and with high expertise and prestige. The Achaemenid Persian Empire stretched throughout the Middle East, north Africa and Asia, and was based on liberal principles of governance. At the time of Cyrus the Great, there were several mechanisms checking the system from an independent military commander, high officials who acted as 'eyes and ears', and special inspectors of central administration to the royal judges who enforced laws 'equally and fairly'; Farazmand (1998). The legacies of early Iranian administrative systems are found in western administration even today.

Chinese administrative tradition also goes back many years. Indeed, the Chinese imperial state lasted for 2100 years, a feat unparalleled in history according to Jacobs (1998). Chosen initially from powerful aristocratic clans, and later through examination, the civil servants were elite and served the Chinese Emperor,

who became supremely powerful. He was, as Jacobs put it, the "supreme political administrator, military leader, chief judge, and religious head. In the West, the church and aristocracies helped restrain the throne, but ... there was no human agency above the Emperor and no independent institution to which one could appeal".

There is little doubt that the accountability of these public servants to higher authorities, whether Persia's rulers or Chinese Emperors, played a huge part in the daily operation of such empires, as well as their historical continuity. Such accountability, however, may have appeared closer to military obedience than anything resembling modern professionalism.

From the perspective of the Westminster tradition, accountability as a concept can be traced, "to the reign of William I, in the decades after the 1066 Norman conquest of England" according to Dubnick (2002:7). In 1085 William required all the property holders in his realm to render *a count* of what they possessed. These possessions were assessed and listed by royal agents in the so-called Domesday Books. This census was not held for taxation purposes alone; it also served as a means to establish the foundations of royal governance ... and by the early twelfth century, ruling was through centralized auditing and semi-annual accounting; Bovens (2006).

Following this, the concept of accountability broadened. Continuing to hold the strong promise of fair and equitable governance, the meaning of accountability was also reversed, so that instead of sovereigns holding their subjects to account, the authorities were gradually held to account by their citizens; Bovens (2006). Karan (2003) notes that the notion of accountability in the Westminster system of government evolved 'primarily from the principle of 'no taxation without consent' established under the Magna

Carta and the principle of “no expenditure except in amounts and ways approved by Parliament” that emerged from the seventeenth-century struggle of the House of Commons to gain control over the executive (Pallot 1992:39). The broad shift from one way financial accountability to a broader construct of public accountability was borne.

Mechanisms to enact accountability of government saw the pioneering elements of political and managerial accountability established by writers such as Woodrow Wilson and Max Weber, whilst notions of accountability for public sector activities were nurtured through later writers such as Romzek and Dubnick (1987), Day and Klein (1987), and Mulgan (2003). Building on such foundations, accountability in western democracies has become a central and pervasive construct. Specific mechanisms for holding elected government members to account, such as Parliamentary Committees, also have a long history. The notion itself goes back to the fourteenth century according to Radice (1999:161). But the history of Parliamentary Committees as a part of government has also been one of instability, given that governments in power have never been particularly happy to establish such Committees; (PAEC (1994:ix). Over time, broader responsibilities for Parliamentary Committees along with a wider array of political accountability mechanisms have progressively evolved.

The pattern throughout history has been for greater complexity to be demanded by citizens as communities have learned more about organizational behaviour and personal frailties in using public power and public resources. In the broadest sense, we have learned that greater public accountability requires power to be dispersed rather than concentrated.

Two other broad considerations little discussed in the public policy accountability

literature and perhaps taken for granted, are the basic mechanisms operating in many liberal democracies; firstly, the separation of powers in which the powers of the executive, the judiciary and the legislative are legally and functionally separate; and secondly, the separation of church and state in governing a secular society. Moskop (1998) advises that the separation of powers, which was one step of the evolution of constitutional government, can be traced back to the writings of Plato's *Laws*, Aristotle's *Politics* and Machiavelli's *Discourses*. It aims to preserve political liberty and the rule of law by preventing the concentration of power.

The United States of America has taken the philosophy of the separation of powers as the underpinning for their system of government. In this case, the constitution limits the powers of government and allocates these powers to different branches; the legislature (Congress); the executive (Presidency); and the judiciary (Supreme Court). As Weatherman (1996:1244) explains, the aim is that ‘no one person or group of political officials may exercise all the political power the government possesses’. The separation of powers therefore formally requires that ‘no individual hold office in more than one branch at the same time’, and that voters elect members of the three branches differently (Wilson 1996:1248). Having said this, there are large “areas of overlapping and shared responsibility that permit the different branches to check and balance one another”, as Weatherman puts it.

Likewise, the separation of church and state, or the constraint against a government either establishing a state religion or interfering in the free exercise of a religion, has also become a fundamental part of modern western democratic governance, whether under a presidential or parliamentary system of government (Van Hook 1998).



## **Accountability Concepts and Models**

One famous concept of accountability for public sector services in Parliamentary systems of government is the notion of 'ministerial accountability'. At first sight, this is a simple but powerful concept. It is the idea that ministers are accountable to Parliament, and ultimately to citizens, for all activities within their portfolio of responsibility. It is based on the idea that a minister develops policy, and separately, the public service administration implements such policy in a neutral and non-partisan manner. The minister can then be logically held accountable for the results of these policies, whilst the public servants ensure that the minister's policies are carried out in an efficient and effective manner when using public resources. So, the line of accountability begins at the bottom with public servants who are accountable to their hierarchical superiors, up through ministers, ultimately to the parliament at the top. These elected representatives also act on behalf of the citizenry and are accountable to them. The concept therefore is one of a straight line of accountability from bottom to top: ministers are accountable for agency performance; department senior executives are accountable for programs and policy advice, and public servants are accountable through ministers to the public.

Despite its apparent appeal, the Westminster model of Ministerial accountability has been complex, and has largely failed to live up to its promise to date. As Hughes (2003:26) noted, although the theory of separation between politics and administration was a major part of the traditional model of administration, it was widely regarded as a myth, and moreover, was 'especially useful for the evasion of responsibility'. The convention of ministerial responsibility in Westminster systems was that ministers are ultimately responsible to

parliament for the actions of their departments and must resign for major departmental errors. But, ministers have increasingly recognized that they should not be the only person responsible for all departmental actions. Thus Hughes (2003:245) concluded, genuine accountability was not possible under the traditional model, and that 'no matter how plausible this seemed in theory, in practice it was a failure'. The reality of this system was that it was aimed at accountability for errors rather than accountability for achieving results. A fuller understanding of accountability was needed.

## **Complex Accountability Notions**

On reflection, it is little surprise that as the size and functions demanded of government have expanded through time, so our demands for government to be kept accountable have become progressively more sophisticated. We have, however, been slow to move away from the central idea of ministerial accountability, though there have been some useful ideas built onto the traditional model. Corbett (1992) for instance provided one such refinement. He argued that as well as upwards accountability to the minister, parliament and ultimately the people, two other forms of accountability also exist: accountability inwards, to a personal or moral code; and accountability outwards, to the community. Corbett's acknowledgement of two additional accountability dimensions was in recognition that throughout the last half of the 20th century, we have been observing increased demands for accountability to the community through mechanisms such as Freedom of Information legislation, ombudsmen, administrative law and the law courts, and have seen the development of various codes of conduct and guidelines to ensure governments were kept honest and accountable. Scott (2006) likewise discusses the notion of three dimensions of public

service accountability; upwards accountability, downwards accountability and sideways accountability.

Not everyone has accepted the failure of the traditional simple 'ministerial responsibility' ethos, however, perhaps because it challenges the notion of a single hierarchy of power and implies power ought be distributed. As late as 1993 official advice was being given at the Australian federal level that the traditional model was still in operation (Management Advisory Board and its Management Improvement Advisory Committee, 1993).

Different kinds of accountability have been emphasized by different scholars; Rubinstein (2005). Stone (1995) provides one such framework in his model of administrative accountability. His model views accountability in terms of five dimensions, with each of these implying a different style of relationship. Stone (1995) sees accountability in terms of five main aspects:

1. *Parliamentary Control*: where administrators support the policy and legislative work of members of parliament. Traditionally entitled ministerial responsibility, this is a superior-subordinate relationship.

2. *Managerial*: where three features are crucial; strategic rather than detailed control, agency self-evaluation (and periodic external evaluation) and a rationalisation of agency responsiveness. This is a principal-agent relationship.

3. *Judicial and Quasi-Judicial Review*: where strict formal standards for decision-making are applied and statutory and administrative rules test the degree of accountability through legal processes such as courts or administrative appeals tribunals. An appellant-respondent relationship is emphasized.

4. *Constituency Relations*: where the concerns of individuals are institutionalized through governing boards, annual meetings of constituents, public hearings, advisory bodies, regulatory agencies, consumer councils or ombudsmen to take up individual grievances and monitor performance. This dimension emphasizes a constituent-representative relationship.

5. *Market Accountability*: where service providers are assumed to be responsive to a body of 'sovereign' consumers who may choose suppliers as well as the quality and quantity of service. A customer-entrepreneur relationship is emphasized here.

Thus, some accountability conceptions are top-down, some are bottom-up and some are outward-oriented. All five of Stone's perspectives of accountability are useful.

As well as these multiple dimensions of administrative accountability, a raft of other political accountability mechanisms exist among a government of the day, the parliament and citizens. One conception of these political accountabilities is the complex accountability model of Coghill (1999). He suggests that, in reality, ministerial accountability operates through a complex accountability 'network' with a wide range of institutions, office holders and network actors being relevant. He also sees both the relationships between each of these network actors along with information flows as influencing accountability outcomes. This is clearly a more complex picture of ministerial accountability. The institutions most influencing the accountability of the Executive in Coghill's research case studies, for instance, included the parliament, parliamentary select committees, the opposition, the parliamentary and organizational wings of the political parties, the Auditor-General, ombudsmen, intergovernmental organizations, the Commonwealth Government, the media,

royal commissions, and the electorate. In this network accountability concept, participants in the network exchange information, and the manner in which each acts is conditioned by ethical norms, competencies and skills demonstrated by individual people such as premiers, opposition leaders and media editorial policy-makers. This complex accountability network idea, therefore, emphasizes the multiplicity of actors, the breadth and complexity of the accountability network itself and the linkages between players. It also stresses the crucial roles played by the media and by independent regulatory bodies.

An important early set of ideas on accountability was also introduced by Romzek and Dubnick (1987). Analyzing the reasons behind the space shuttle Challenger disaster in January 1986, they identified four types of accountability. To them, the four primary accountability dimensions were; hierarchical accountability, legal accountability, professional accountability and political accountability. Their thesis was that NASA had previously been an organization where professional accountability had prevailed, but that pressures to develop a politically responsive agency gradually became dominant over the technical culture. The reliance of hierarchical and political accountability systems over professional accountability systems produced circumstances in which the Challenger disaster eventually occurred. A parallel conclusion confirming the importance of professional accountability was also reached by Gregory (1998) in his analysis of New Zealand's 'Cave Creek tragedy', where 14 people died when a viewing platform collapsed.

These observations of accountability models have also been made within the context of broader frameworks offered by authors such as Rubinstein (2005) and Bovens

(2006), both of whom suggest multiple overarching accountability dimensions. As well, the broader discussions of Behn (2001) and Mulgan (2003) emphasize the complex accountability challenges arising in public governance, whilst Dubnick (2005) identifies the disappointing lack of empirical evidence underpinning accountability research compared to the more common ideological or rhetorical stance taken.

In terms of framing accountability, these accountability models have several implications for how we frame the concept.

### *Public Accountability*

First, the very definition of public accountability has remained slippery and contestable. Along with the growth of broader meanings to accountability, public accountability has also grown to become many things to many people. Indeed, borrowing Christopher Hood's (1991) phrase, public accountability has almost become a "label for all seasons". When we disagree with anything in the public realm, the appeal is for more public accountability. So is public accountability, as Karan (2003) suggests, "simply constitutional (ministerial) accountability?", or perhaps everything political, carrying with it, as Mulgan says, "most of the major burdens of democratic governance"? (Alvins 2004:3). Whilst this is probably going too far, it is like 'the public interest', which is itself defined and re-defined through continual discourse in the polity, and which is tailored, in the end, to mean whatever citizens want it to mean. Public accountability, likewise, remains understandably broad and contestable while it evolves. As Alvins (2004:12) stated, "public accountability is the form of the accountability relationship where the public—citizens, the community at large, the governed—are the account-holders, the external 'other' scrutinizing and calling to

account those exercising public or governmental power or undertaking public or governmental functions—most commonly elected and appointed government officials, but also others acting in the public sphere”.

This is no longer a “simple model of accountability in which a single account-holder holds a single accountor to account for a clearly defined task” (Mulgan 2003:22) but a “densely plural relationship of many account-holders to many accountors, for a huge array of tasks, functions and responsibilities, many of which are not at all clearly defined, and where the calling to account is done not directly, but via many accountability agents, intermediaries, institutions, mechanisms and processes”. Or in the words of Bovens (2006), public accountability has an expectation of openness to the general public in regard to “matters in the public domain, such as the spending of public funds, the exercise of public authorities, or the conduct of public institutions” ...even extending “to private bodies that exercise public privileges or receive public funding” (Scott 2000:41). Overall, then, “public accountability is accountability in and about the public domain” (Bovens 2006:12).

### *Imperfect Ministerial Accountability*

Second, we could observe that the traditional Westminster idea of ministerial accountability operates better in theory than in reality. Any viewing of modern Parliamentary practice rarely sees Ministers resigning – even in the face of monumental disasters in their portfolios. Importantly, though, it is equally evident that the notion of Ministerial accountability, and the requisite Ministerial resignation in the face of portfolio problems has never, in fact, operated well. Finer (1956:393) for instance observed over forty years ago that ministerial resignations were not only “rare, but arbitrary and

unpredictable”, whilst Webb (1920) had earlier warned that they were “illusory as an instrument of democratic control”. Little wonder then that Lewis and Longley (1996:503) labeled ministerial responsibility as “a ruling fiction whereby ministers shelter behind civil servants and vice versa” (Barberis 1998:453). Ministerial resignations, when they do occur, seem to be more the result of losing the confidence of Ministerial colleagues than about accountability to citizens (Marshall 1991:464).

Woodhouse (1994:v) has also commented that whilst ministerial resignations have a constitutional basis, they have not always fulfilled the constitutional requirement in the sense of ‘giving an account’, and that indeed, at times the very resignation of a minister seems to have been a means of evading such accountability. Notwithstanding this, Woodhouse (1994:174) argues that the convention of ministerial accountability is likely to remain a symbolic feature of British political accountability, albeit not as strongly practiced as voters might wish.

Perhaps the broader issue here is how society holds elected representatives to account, whether in a presidential, Westminster or any other democratic context. This is no simple matter and depends on political culture. Scandinavian countries, for example, perhaps have a reputation for strongly democratic governance, and certainly boast representative parliaments. But Arter (2004) also sees these parliaments as relatively closed to the public, despite the region’s reputation for openness. Nordic countries, as consensual democracies, exhibit a “culture of consensus and structures for conciliation and arbitration” (Arter 2004:582). In such a consensus democracy, where the opposition participates in the exercise of power, perhaps some attenuation in the lines of accountability of governors to voters is understandable. And in jurisdictions

such as Sweden, “State agencies fall under the authority of the cabinet, and not under an individual minister responsible for a particular policy area”, according to Bergman (2004).

Another aspect of political culture is how ministers act when matters of accountability are raised. The fusion in which political power is concentrated in the legislature in, say the British Parliamentary system, results in strong party discipline in order to keep the Prime Minister in office compared to systems such as the US, where Congress members are freer to vote according to their own beliefs; Wilson (1996:1250). Such real world party political incentives cloud attempts to keep Ministers personally accountable to the citizenry.

### *Complexity of Accountability*

Third, the accountability concept is clearly now a complex undertaking. In contrast to the simple sounding notions of personal accountability and of ministerial accountability, multiple dimensions are relevant within a series of sophisticated and interlinked accountability ‘networks’. This complexity works at several levels. We might cite on the basis of the brief review above the dimensions of; political, managerial, market, judicial/quasi-judicial review, constituency relations, and professional accountability. And each of these dimensions comprises a complex network. Thus, what appears to exist in terms of accountability mechanisms nowadays are overarching networks of political accountabilities for parliament and the government at the highest level, underpinned by other networks such as Stone’s administrative and managerial networks, Romzek and Dubnick’s professional accountabilities and complex networks of independent regulators and Ombudsmen.

These accountability dimensions operate through multiple mechanisms ranging from financial audit, managerial reporting, and democratic voting at elections, to Parliamentary Committees, as well as through the media, customer feedback and many other accountability channels. Importantly, these arrangements also involve a wide range of different institutions with differing roles. And whilst some accountability institutions are clearly part of the democratic fabric and have direct accountability to citizens, there has been a rise in the importance of independent institutions of public accountability (through roles such as independent regulators and ombudsmen) whose accountability is diffuse. Of course, the very notion of government also has complexity today given that it includes institutions ranging in role from those at the heart to the traditional public services to those more clearly in commercial operation, yet publicly owned, as well as institutions having a myriad of other objectives ranging from regulation, monitoring, review, policy advice and service provision.

These ideas are consistent with those of Scott (2000), who noted that the contracting-out of services had left service providers not directly accountable to Parliament any more and that accountability was “premised on the existence of complex networks of accountability” based “upon interdependence and redundancy in which overlapping mechanisms reduce the centrality of any one of them”. Rubinstein (2005) in the United States endorsed Scott’s idea of “dense networks of accountability”, saying simply that “in the post-liberalised state, accountability has become very complex. An agency is required to answer to many actors, and achieve many goals.”

Likewise, these complex accountability ideas are also consistent with those of Freeman (2000), who observes what she terms a “depressingly messy picture of

administration” in the United States. Citing examples of health care service delivery, she argues that this is “a new and more accurate description of governance as a negotiated enterprise’ made up of “a variety of actors making collections of decisions in a web of relationships”. Freeman sees the reality of today’s public services as being characterized by shared governance between public and private actors in the delivery of services, and argues that this requires, as a consequence, multiple and overlapping checks in order to produce sufficient ‘aggregate accountability’ to assure its legitimacy.

### *Accountability Blurring*

What’s more, and fourthly, Freeman’s notion of shared public-private governance also suggests blurred lines of accountability. They are neither purely public nor purely private. Whilst some of this blurring has even become accepted as ‘best practice’ through formal government policies such as public-private partnerships, it has a much longer pedigree. In another blurring of accountability lines, Marshall (1991:468), for instance, noted that the Next Steps agencies in the UK were in the 1980s established on the one hand as independent of department control through their framework agreements with their agency heads (as accounting officers) accountable to Parliament and to the Public Accounts Committee whilst on the other hand suggesting that “the present structure of ministerial responsibility through ministers is not to be changed”. Marshall suggests that “the reconciliation of the contradiction lies in the distinction between formal or legal accountability and practical accountability.” We might also note the lengthy history of the public-private mix (Wettenhall 2003).

### *Trade-Offs with Accountability*

Fifth, to the degree that reforms are being accompanied by an array of different

mechanisms for accountability over the traditional ministerial accountability assumption, there is much potential for trade-offs to occur. The history of accountability improvements have always seen trade-offs being made. Viewing accountability in terms of just four dimensions (hierarchical, legal, political and professional) Romzek and Dubnick (1998), for instance, observed that those favouring hierarchical accountability ask for priority to be given to supervisors and top organisational officials (for example by way of performance reviews), whilst those favouring legal accountability ask for priority to be given to constitutional principles, laws or contractual obligations (note for example the anti-corruption investigations in Italy in the mid 1990s). Those favouring political accountability ask for priority to be given to responsiveness—external groups, markets or voters (for example by way of community-based policing), and those favouring professional accountability ask for priority to be given to best professional practices (for example, deference is granted to engineers when designing roads, bridges and aeroplanes). In this light, the suggestion by Hodge (2000, 2004), that perhaps trade-offs are implicitly being made as we have introduced reforms such as contracting-out is not in retrospect so surprising. Likewise, Bovens (2006) describes the evaluation of accountability as a somewhat equivocal exercise in view of the fact that accountability arrangements may score well on one dimension but not on others, and may even not always point in the same direction. Furthermore, the question of sufficiency arises, in that there can never be enough accountability, rhetorically speaking.

### *Conceptualising Accountability Amidst Complexity*

Sixth, we might conclude that a central difficulty in researching accountability is the

issue of how best to frame public accountability in terms of the multiple competing models and perspectives that seem relevant in this arena. One way to marry up the various public accountability models is to adopt, as did Mulgan (2003), the simple taxonomy of four questions; Who is accountable?; for what?; to whom (or what)?; and how (or through what mechanism)? Drawn from Barberis (1998), and presumably other previous management writers over time, these questions neatly tie together most of our accountability concerns. We could complete this overarching framework of four questions by adding the issue of the forum adopted and the consequences or sanctions applied.

Another way to marry up the various accountability models is to conceive of a pyramid of accountability practices, in much the same manner as did Ayres and Braithwaite (1992) when conceptualizing real world regulatory practices. Thus, legal accountability requirements might feature at the top of the pyramid, but below this, (and paralleling the regulatory pyramid concept), most of the mechanisms for ensuring public accountability in practice come from less formal practices, conventions and expectations - both codified and informal.

Likewise, Bovens (2006) suggests that accountability can be framed along four dimensions; the nature of the forum (whether political, legal, administrative, professional or social); the nature of the obligation (whether vertical, diagonal or horizontal); the nature of the actor (whether corporate, hierarchical, collective or individual); and the nature of the conduct (whether financial, procedural or product related).

### **Accountability Trends**

Throughout the nineteenth and twentieth centuries, governments moved away from the nepotism, corruption and poor skills which had previously characterised public systems,

towards cleaner and fairer bureaucracies. Over recent decades, three trends have since occurred; managerialism, contractualisation and privatization—all part of a broader movement labelled “New Public Management” (NPM). This move away from the traditional public administration model has included; smaller production units, contract based competitive provision, stress on private sector styles of management, formal standards and performance measures, an emphasis on output controls, being closer to customers, and a reduction in the scope of government along with changed interactions between public sector managers, elected politicians and the public. One well known philosophy here has been the phrase “steering not rowing”, coined by Savas (1987) and made famous through Osborne and Gaebler (1992) in their agenda to “reinvent government” in the US. Under NPM, public sector work evolved from an administration with a tendency to avoid risks to an ethos in which incentives were geared to enable managers to deliver “results”.

Greater use of market and commercial techniques has therefore occurred in public sector operations. Through either formal legal contracts or informal quasi-contractual arrangements, most areas of government operations have progressively seen service outputs agreed and commercial penalties applied for poor quality provision. From a European perspective, Lane (2000) for instance, argues that the use of contracts in the public sector is now extraordinary in its comprehensiveness with contracting becoming “more important than the traditional tools of government when co-ordinating the public sector.” Competitive tendering and contracting systems are now common through to the more recent adoption of public-private partnership arrangements for the provision of large infrastructure facilities (Hodge & Greve 2007).

Parallel to these trends has been the progressive “privatization of the state”, as governments have embarked on programs to sell-off public enterprises (see Hodge 2000; Parker 2004; D’Souza & Megginson 1999; and Cook & Kirkpatrick 2003). This trend has also been accompanied by a global move to initiate new accountability regimes including sophisticated independent regulatory regimes charged with minimizing consumer prices, maintaining high service quality and ensuring the continued economic viability of essential services such as electricity or water.

All of these trends have had profound influences on public sector accountability systems. And they have seen much academic debate. On the one hand, the simple view that accountability must have been increased following the adoption of managerial, private sector contracting or enterprise sales reforms is understandable, since work is no longer now submerged in the depths of bureaucratic government ministries. Better specification of outputs, monitoring of actual costs and the ethos of competitively procuring and then paying for services when delivered have all certainly been useful principles in changing traditional organisational culture.

But positive assessments have not always occurred. There has been a persistent failure to effectively resolve several issues around contractualisation concerning transparency and accountability. Many of the broader accountability mechanisms that have traditionally operated in the public sector – such as Ombudsman reviews, Freedom of Information, scrutiny by the Auditor General, Administrative Law and ministerial responsibility—have been at risk of being stripped away under contracts. This leaves, as Taggart (1992:371) coined, an “accountability vacuum which the courts may be drawn into”. Highly relevant here as well is the issue of secrecy and disclosure, including access to information under contractualisation, and the

practice of appealing to ‘commercial-in-confidence’ to shield reforming governments from disclosing contract information. In such instances, the public see the use of commercial-in-confidence as little more than a ‘figleaf’ behind which governments hide. Moreover, regular parliamentary scrutiny has been reduced and the involvement of citizens is increasingly being tested, in either the polity or as a customer. Overall therefore, public accountability appears to have been a casualty. Importantly, governments continue to be held accountable by citizens for all services, whether divested or contractualised, despite attempts at shifting blame for service failures onto contractors or privately owned firms.

There has certainly been a ‘changing of the guardian’ from one where a simple but idealistic accountability regime reigned to a new situation in which a more focused but complex series of networks now act as guardians for public accountability (Hodge 2004). All this, though, has been part of a broader philosophical shift in governance around the globe. Majone (1996) observed “the rise of the regulatory state”. One part of this was an explosion in the number of independent regulators accompanying the privatisation of state owned enterprises. But regulatory practices nowadays continue inside government, as well as outside, across national government boundaries, in hybrid institutions that cross the private-public divide, and through self-regulation; Minogue (2006:69). Scholars now therefore label networks of governing bodies as a broader “regulatory state” (Sunstein 1990); as “regulatory governance” (Minogue 2004); or as “regulatory capitalism” (Levi-Faur & Jordana 2005). All view this broader conception of regulation as a fundamental reordering of priorities & power, rather than just rearranging traditional command and control rules. A uni-centric and hierarchical



model of government has been replaced by a “horizontal government” which acts more as a partner, co-regulator and co-actor in the governance game (Michels & Meijer 2008).

There is now a huge array of accountability bodies, and we have also granted more power to output specifications and legal contracts, and increased trust in private commercial incentives to manage commercial risks for performance. Not only have public accountability guardians changed in the institutional sense under today’s philosophy of regulatory governance, but there has also been a change in what we as a society expect of our guardians and our governments as well. Our community expectations have increasingly demanded a new ‘results-oriented accountability’ regime in addition to previous concerns focusing on procedures, due process and honest financial dealings in the public domain (Barrett 1999; Mulgan 1997).

### **Effectiveness of Accountability Arrangements**

Our modern public accountability arrangements are now clearly very complex. Different governance systems will provide differing incentives for governments to remain accountable. Parliamentary systems, for example, will through their design, enable simple majorities to control policy formulation on behalf of citizens. And presidential systems may provide better safeguards for minority interests; Weatherman (1996). And at a lower level, numerous mechanisms to maintain accountability will exist. Mulgan (2003), for instance, illustrates multiple mechanisms for public accountability in the case of a Westminster system.

Any assessment of the adequacy of accountability needs to be undertaken through the lens of why public accountability is important in the first place. Bovens (2006) reminds us that accountability arrangements

firstly help in providing sufficient information about the manner in which democratically elected agents are undertaking a policy agenda. Second, through public accountability forums that are visible, tangible and powerful, accountability contributes to the prevention of corruption and the abuse of powers. Third, accountability ought also enhance the learning capacity and effectiveness of the public administration. And behind these, accountability helps to ensure that the legitimacy of public administration remains intact.

Managerial reforms have no doubt left public sector employees, often under performance contracts and closer performance scrutiny, far more sensitive and even compliant to the political wills of their masters. This confluence of interests has produced a public service more effective in delivering governments that are able to act quickly, and that can better deliver political promises or policies than traditional administrative techniques. But they may also have helped governments to look good through consummate media management, and better able to claim all political successes whilst escaping the appearance of any accountability for government policy failures.

Many accountability arrangements in the public realm will be recognized as simply the other side of the coin stemming from a changed philosophical approach to meeting the public interest through ‘regulatory governance’. Each of the accountability lenses discussed earlier will assist in evaluating the effectiveness of alternative accountability regimes, as well as the simpler models of Bovens et al (2008) who suggested democratic, constitutional and learning components of accountability, and Mashaw (2006), who saw the components as public governance, markets and social accountability.

What is also crucial here is to acknowledge that evaluations of

accountability are fraught with personal values and judgments and need to be tempered in the knowledge of real limits to accountability. "In the end the assessment of accountability cannot be separated from the vision one has about what constitutes adequate democratic control, sufficient checks and balances, or good enough governance", as Bovens (2006) nicely put it.

So, extensive advocacy on the one hand, and criticisms on the other, will continue for all public accountability mechanisms. There is little doubt, for instance, that Parliamentary Committees have helped hold government to account in the past and that voters have seen them as serving a useful purpose. On the other hand, Young (1997) quips that they are little more than 'a collection of the unfit appointed by the unwilling to perform the unnecessary'. A wide range of public accountability mechanisms is similarly likely to be debated. In this vein, a crucial question is the degree to which we are suffering from an 'accountability deficit', as claimed by critics such as Fisher (2004), or whether those in the public arena are in fact over-regulated (Lahey 2005) and weighed down by an accountability overload (Brennan 1999). Another debate will involve the question of how best to make accountable regulators and other independent bodies at arms length to government so that the public interest is served; House of Lords (2004). Notwithstanding, we will remain much more focused on questions of accountability than we have ever been in the past, particularly in what some now see as a risky environment.

## Conclusion

The concepts of accountability and of public accountability are central to democratic political processes, but also remain slippery and ambiguous. Today's multiple networks of public accountability are the result of a lengthy history in which we have learned

through the polity how to control personal and organisational frailties as public power and public resources are utilised for political purposes.

No doubt claims of accountability crisis will continue in the twenty first century, as Dowdle (2006:26) suggests, simply because there is a foundational contradiction between our innate desire to trust others and the innate limits in our capacities to trust others. Accountability in the public realm will indeed as he says be both maddeningly fragmented, as well as extraordinarily promising. And the role of transparency in improving public accountability in an age of regulatory governance will be increasingly debated along with measures to ensure the legitimacy of independent regulatory institutions (Hood & Heald 2007).

A wide range of mechanisms in which all actors are required to give account of their conduct will continue to guard against the abuse of power, prevent corruption and improve governance. Public accountability will continue to underpin public trust. No single template or perspective is likely to capture all the intricacies of future accountability requirements in the public realm, however, and new ways of balancing the legitimate accountability demands of citizens, government and businesses will be sought.

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## Anarchist Governance

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### **Introduction**

The word Anarchism comes from the Greek “an”, without, and “arch or archaism”, rule or ruler. Anarchism advocates the elimination of all forms of imposed authority. Some have made the word synonymous of disorder or chaos, trying to invest it with fearfulness. However, Anarchism defends the possibility of order without government. Actually, for anarchists, it is authority the one who creates disorder (Woodcock 1944). There is considerable variation among anarchist political philosophies. Bibliography and opinions differ in areas ranging from the role of violence in fostering Anarchism, to the preferred type of economic system, or the interpretation of egalitarian ideals (see Nettlau 1934, 1935; and Bettini 1972)

Anarchism has a strong utopian base—some utopian socialists, like Godwin, were anarchists. Anarchists disagree with Hobbesians and generally assume that individuals are sociable and naturally good or neutral.

For anarchists, authority is oppressive: it suppresses individual free actions in benefit of other persons' decisions. Although these decisions could be said to be in the true interest of the people, they deny and annule human being's liberty and personality. As Rousseau said, the fact that each person depends on all others does not degrade human nature. Conversely, the fact that a person depends on the arbitrary orders of others and lives according to their opinions denies human essence and natural independence.

According to anarchists, the State is not synonymous with Society. The first is a manipulating human artifice; the second is natural. The State has its origin in the deceit of the rich toward the weak. Government is

an exploiter by definition. Its power is based on war, territorial expansion and booty, not on a conception of natural social unit. Anarchists do not believe in the origin of government on a social contract. Therefore, the disappearance of the State will not affect the society or the civilization. In a context of freedom, self-control could replace the control from above since good behaviour will become instinctive and spontaneous. The anarchist society is thus a natural organization based on free commerce and a constantly changing order (Gómez Casas 1986).

So, for anarchists, the problem is not the human being in himself, but government, law and private property, that is to say, the institutions of authority. Law is an instrument of the government that tries to protect and preserve private property. It is a class weapon. It inhibits rational moral judgment and it limits freedom (see Carter 1971 for a study of Anarchist political philosophy).

### **Contradiction with Political Action**

In principle, anarchists do not believe in political action. They do not side with a political party. Politics can only seek power, repeating the cycle "oppressors-oppressed". Thus, the government can only be abolished by non-political means. This attitude is, in many occasions, paralyzing. It can lead to individualism. Actually, Herbert Read (1940) maintained that individualism is possible only in a complex anarchist society with an elaborated division of labour. A capitalist society is a precondition for the development of anarchist ideas on individualism.

Nevertheless, Anarchism usually seeks self-realization within the framework of society, not the liberal self-difference, supported in wealth. Therefore, it looks for satisfaction in "non-economic" terms. In economic terms, mutual dependency is assumed. Still, creative work and co-operative pleasure generate satisfaction.



Mutual dependency makes anarchists reject free-riders. Work is the source of the social value, the individual satisfaction and the moral virtue. Anarchists usually establish a moral obligation to work.

Since political action is not considered an advisable means of change, anarchists give special importance to the moral change based on education (see Godwin 1793). When educational standards increase, the strength of authority decreases. Education systems must be made polytechnic and avoid authoritarian methods.

Other anarchists defend the change through propaganda or violence (e.g. Richards 1977). Direct action has an exemplary nature. It intensifies the popular sensation of oppression and boosts action, prevented by routine. Many defenders of violence shield themselves behind the idea that "the system", not a particular person, is their target. So, they justify means by their supposed consequences on an imaginary system. Violence is criticized by many other anarchists (see Hennacy 1994).

### **Differences from other Libertarian Trends**

Anarchism can be distinguished from Liberalism: although both seek freedom, the liberal ones accept a minimum State as a referee between individuals. For liberals, freedom is synonymous with choice, only limited in monetary terms. Conversely, Anarchists talk about freedom in a context. Freedom emerges in free inter-subjectivity: I need others' freedom to be able to be free myself. In classic liberalism, this is not always necessary.

Anarchists also refute the principles necessary to sustain conservatism from the theoretical point of view. The intrinsic equality between people makes possible a society without leaders. Besides, tradition does not always increase wisdom. It is based on authority and on the compulsion and nostalgia of the past/fear of the future.

Anarchists are against the competitiveness of social Darwinism and look for an artificial, deliberate and conscious cooperation that constitutes a defence against the potentially authoritarian character of the State.

### **Some Precursors of Anarchism**

The first known usage of the word anarchy appears in the play *Seven Against Thebes* by Aeschylus, dated 467 BC. Within Greek philosophy, Zeno's vision of a free community without government is opposed to the state-Utopia of Plato's Republic. Like many modern anarchists, Zeno believed that if people follow their instincts, they will have no need of law courts or police, public worship or use of money. Conversely, in Athens, Plato and Aristotle used the term anarchy disparagingly. For them, it was associated with democracy, which they mistrusted as prone to deteriorate into tyranny.

In English speaking countries, anarchist ideas and practices initially developed within the radical Whiggery and Protestant religious dissent. The Anabaptists of 16<sup>th</sup> century Europe are sometimes considered to be religious forerunners of modern Anarchism. According to Bertrand Russell (1945:20), Anabaptists "repudiated all law, since they held that the good man will be guided at every moment by the Holy Spirit [and] from these premises they arrive at communism".

The first modern author to have published a treatise explicitly advocating the absence of government is William Godwin (1793). Though he did not use the word Anarchism, some regard him as the founder of philosophical Anarchism. The term "anarchist" was used during the French Revolution as an insult against the left. However, as American political society developed along the liberal model, anarchist thoughts were expressed in America in the



writings of Henry David Thoreau (1905) (see Martin 1970).

### **Policies Defended by Proudhon**

But it is not until the French Pierre-Joseph Proudhon published in 1840 *What is Property?* (Proudhon 1876) that the term “anarchist” was adopted as a self-description. For this reason, some claim Proudhon to be the founder of modern Anarchist theory and, in any case, a model for Anarcho-communism.

Proudhon was philosophically individualistic. He defined anarchy as the government of each one of itself and by itself, fortified by the public and private conscience and the mutual moral monitoring. There is no freedom without self-control. Thus, freedom is not ‘any’ absolute freedom. It is a Kantian duty, understood in terms of ought, that will be born spontaneously in an anarchist society.

On the basis of its opposition to any obstacle that limits individual freedom, Proudhon condemns all forms of the State, be they representative democracy, authoritarian socialism, etc. He proposes a “self-managed socialist federalism”. A federation of egalitarian self-managed communes will give rise to a decentralized familiar and local society, where men would learn to value moral virtues.

Proudhon considered the farmer the example of self-sufficient individual existence. So, to create an order without dependency and domination, he defended the establishment of communities of self-sufficient farmers. In the industrial activity, dependency and domination can only be avoided through “contractualism” or “mutualism” (see Swartz 1927). This is free association on the basis of multiple contracts that regulate social actions. In Capitalism, a just contract is not possible since an antecedent property exists. But Proudhon imagines a contract without property.

However, the system of production is not as important as the way in which the wealth circulates. The currency is dominated by the “egoistic control of the financial capital and the capricious control of the State”. We have to establish explicit federal or communal mutual contracts instead of individual contracts based on money. Banks must act as great centers of cooperation between producers and give credit without interests. This monetary organization would be based on a system of reinsurance. Mutual credit and labour checks of the *People’s Bank* would be given. Money would reflect the value in hours of labour incorporated in each product. We must say however that, although in this system the concession of credit would be almost limitless, Proudhon did not worry about the possibility of inflation or the way to maintain the credit.

Proudhon does not defend an equality of results, but an “equality of opportunities”. He condemns the property right if the proprietor can live without working, from his interests, rents or unearned income. Proudhon (1888) defined in 1847, before Marx, the surplus value of capitalists. Taking advantage of the division of labour, capitalists pay the individual efforts of their workers, not the value of the collective effort of the workforce. But, as opposed to Marx, Proudhon did not believe in the importance of the class struggle nor in the inevitability or historical necessity of socialism. In addition, socialism would not be imposed from above by the governing class.

Finally, Proudhon rejects violence. He feared the role of intellectuals in social movements. Only moral persuasion, education and propaganda, together with passive resistance to illegitimate government, can lead to social transformation. In fact, Proudhon himself was sent to jail for resisting government (Zoccoli 1908).

## Socialist Anarchism

The *International Workingmen's Association*, at its founding, was an alliance of socialist groups, including anarchists and Marxists. Both sides had a common aim (stateless communism) and common political opponents (conservatives and other right-wing elements). But each was critical of the other. The conflict between the two groups led to an endless argument between Bakunin, representative of anarchist ideas, and Marx. In 1872, the conflict in the First International reached its peak with the expulsion of Bakunin and those who had become known as the "Bakuninists" at the Hague Congress. Later in the 19<sup>th</sup> century, Bakuninists built on the Marxist critique of capitalism and synthesized it with their own critique of the state. Bakuninists emphasized the importance of a communal perspective to maintain individual liberty in a social context. They also stressed the critical role of workers self-managed organs of production and consumption.

Mikhail Bakunin wanted to carry out a revolution to make capitalist institutions collapse. Property rights are based on conquest and inheritance, which make the existence of misery and ignorance of the masses possible. He rejected Marxist political use of unions and parties and collectivism on large scale, that would lead to a nationalistic state capitalism. In order to eliminate centralization and nationalism, Bakunin defended the existence of small interdependent communities with different functions and linked through weak bonds. Federal power would be reduced to a minimum and controlled by the delegates of the community. Bakunin opposed the proletarian dictatorship. A dictatorship cannot be the seed of freedom. The State of the proletarians would not be extinguished: like every other organism, it will seek its survival.

On the basis of an environmentalist theory and a certain social determinism, Bakunin says that human psychology is the fruit of education. He defended education as a means of transformation of society, education understood as making the proletarians aware of class struggle and of their possibility to begin the revolution. However, in the course of time, and after his collaboration with Nechayev, Bakunin also defended violence and conspiracy as a political instrument.

Bakunin's concept of freedom is complex. Freedom is a quality of the mind released from self-interest, source of mistakes and lack of social harmony. First, to govern others destroys my independence and self-realization, which requires the recognition of my peers, in whom I am reflected. Secondly, freedom is not the possibility of satisfying desires, but liberty of reason or opinion. In a social community, it can only be achieved if individual reason is previously forged by society or if there is a "right natural reason". So, there is a necessary connection between individual freedom and the social unit.

Bakunin is not so idealistic with regard to work. People work to survive, not for pleasure. The only way to avoid the *free-rider* problem is through moral disapproval. The one who does not want to work must be divested of his political rights. Moral duty even allows letting him die out of hunger. According to Bakunin, people must receive goods according to their effort. Thus, as opposed to Proudhonian "equality of opportunities", Bakunin defends an "equality of treatment".

Contrary to the "equality of treatment", defended by Bakunin, Peter Kropotkin defends "equality of satisfaction" or distribution according to needs. A follower of Bakunin, Kropotkin explores in 1902, in *Mutual Aid: A Factor of Evolution* (Kropotkin 1914) the utility of cooperation. As opposed to social Darwinism, cooperation is

considered more successful than individualism. Kropotkin establishes parallels between human and animal societies and tries to prove that the natural human organization consists of small communities with cooperation. Kropotkin condemns national borders and the centralized State as opposed to nature. Here, we see that Anarcho-communism emerges from scientific theory based on evolution.

Although some anarchists, like Tolstoi, wanted to eliminate urban industrial life, Kropotkin accepts the irreversibility of industrialization. But he wanted to make rural and urban life compatible. His ideal is an organization of small communities, like the watchmakers of Swiss Jura. Like Bakunin, Kropotkin defends that the State, capital gain and the wage-earning work constitute repugnant bonds that must be destroyed. He proposes a peaceful transformation, considering violence justifiable only when it tries to compensate for the use of force by governments.

### **Current Types of Anarchism**

Although Anarcho-communism is the most influential type of Anarchism, there are other important examples of Anarchism today. Apart from Anarcho-communist, we shall briefly analyse here Anarcho-Capitalism and Anarcho-Syndicalism.

First, Anarcho-communism or the libertarian left influenced the radical movements of the 60's and beginnings of the 70's (the student revolts, the hippie movement of 1968 in France and U.S.). Philosophically, this ideology is nourished by Marcuse's theory, based on the concept of alienation but the rejection of Marxism-Leninism. Spontaneous action is a liberating path to avoid consumerism in capitalism. Authority is everywhere. Only the individual or small communities can escape from it, creating a safety cord between them and

corrupted society. A moral optimist with regard to educated man is needed in this theory, as moral subjectivism makes freedom impossible.

Left-wing anarchists generally believe that governance resides with the community at a decentralized level. In this stance, Karl Polanyi (1957) defends the replacing of many markets with community markets and non-anonymous institutions that are embedded in reciprocity and redistribution. Consumer goods markets are embedded in social norms, but labour, money and land markets resulted from violent intervention of the state. In liberty, differing economic formations could peacefully coexist. In particular, as citizen education is an essential condition for participatory democracy, democratic decision-making should be introduced in families, community groups and business organizations (see Stanfield 1986).

Some feminist groups, which consider authority a masculine concept, resist authority in these terms. Specifically, Anarcha-feminism, a concept allegedly created during the 1960's but associated with early 20<sup>th</sup> century theorists such as Emma Goldman and Voltairine de Cleyre, is a kind of radical feminism. It believes that patriarchy is a fundamental problem in our society. In the Spanish Civil War, an anarcha-feminist group, "Free Women", was organized to defend both anarchist and feminist ideas (see Gómez Tovar and Paniagua 1991).

Secondly, from the right wing, many free market adherents believe in anarchist system where individuals freely operate with others in a decentralised manner, without authority structures such as governments and large corporations impinging on them. Anarcho-Capitalism demands the abolition of the state and the control of the economy by individual and entrepreneurial monetary assets. In principle, this anarchism is not egalitarian. It rejects State coercion, but it omits criticizing

any economic coercion arisen from *laissez-faire*. Defence of an unrestricted kingdom of capitalist consumption is generally based on moral subjectivism.

Nozick (1976) defends a State with solely a tutelary function of enforcing property rights. Murray Rothbard, basing himself on the idea of natural rights, tries to demonstrate, as Ayn Rand had, that, given a demanded commodity, production can be assumed by a private company. Therefore, he pleads for the unrestricted freedom of the individual on the basis of his Austrian School view (see also Jasay 1989).

Thirdly and finally, Anarcho-syndicalism or revolutionary syndicalism defends industrial violence, as opposed to the passive and non-violent attitudes of Anarcho-Socialists. This movement bloomed in nineteenth century France, 1890-1920 Russia, and 1930s Spain (especially in the Civil War, 1936-39). George Sorel (1915), one of the principal defenders of revolutionary syndicalism, gave an expressive and educative function to violence. It responds to capitalists' and State violence. General strike can be used as a myth to terrify politicians. Sorel was partly Marxist, but he eliminated the catastrophic nature of the transition to socialism. This transition could not be explored by the "scientific" theory. Sorel's theory was taken up by Nazism and fascism, a coherent outcome of his aesthetic vision of violence.

Revolutionary syndicalists claim that the administrative aspects of the unions' life prevail over the revolt instinct over the course of time. The 1906 Confederal Congress of Amiens defined the strategy of the movement. The militants declared themselves "anti-suffragettes". Politics should be eliminated from the union. They defended "direct action", like boycotts, workers refusing to buy their bosses products; or sabotage, i.e. to work deliberately inefficiently, mistreating the

product or the machines. Unionists should make their own commodities. Finally, the strike was considered the main weapon. It could lead to a general strike, the instrument of the revolution.

From 1890, French employment agencies followed the anarcho-syndicalist criteria of the CGT, the *Confederation Générale du Travail*. This French union was the model of the Italian revolution after World War I and of the Spanish Civil War. In the Spanish Civil War, a majority of the population affiliated with the CNT, the revolutionary *Confederation Nacional del Trabajo*. Other major anarcho-syndicalist organizations include the *Workers Solidarity Alliance*, and the *Solidarity Federation* in the UK.

In the United States, many new immigrants were anarchists. A large number of them were Jewish immigrants who had left Russia and Eastern Europe during the late 19<sup>th</sup> and early 20<sup>th</sup> centuries. So, the North-American *Industrial Workers of the World*, created in 1905, was based on an anarchist philosophy. The Anarcho-syndicalist orientation of many early American labor unions played a large part in the formation of the American political spectrum. The United States is the only industrialized former British Colony to not have a labor-based political party.

Conversely, in Latin America a political Anarchism grew. It is the case with Mexico. There, anarcho-syndicalists like Richard Flores-Magon led various revolts and uprisings to overthrow the dictator Diaz, influencing also the modern day Zapatista rebellion (see Schuster 1931).

## **Anarchist Economic Policies**

### *Self-Management*

The anarchist notion of "self-management" is a revolutionary idea. It implies a radical change in the situation of workers who may break with subordination to an external

power. Their status is transformed from simple salesmen of their workforce to becoming their own employers. Maire and Julliard (1975) define self-management as the direct intervention of individuals and groups in fields where their own future is at stake. So, self-management is not only an economic doctrine, but also a philosophy of direct action and participation in all aspects of life. In economic terms it defends the abolition of the wage condition. It implies also the creation of horizontal social relations, groups and institutions and the reduction of vertical relations from the cupola to the base. This assumes avoidance of any delegation of power. Society cannot be divided into those who create and control and those who have no possibility of creation and direction of their life (Bertolo 1984). Rochdale (in 1884) and Boimondou (in 1941) defended cooperativism as a way of industrial self-management. Charles Gide (1847-1932) proposed a consumer cooperativism to avoid Capitalism consumerism. Georges Fauquet (1883-1953) explained that not only in Capitalism, but also in Communist countries labour and consumption are used as means. We must erase the distinction between consumers and producers.

A cooperative society is supposed to be a "service economy". Both self-managed and capitalist companies assume a risk. But, in the cooperative company, partners provide a service without profit eagerness. This type of organization has theoretical advantages and disadvantages. As an advantage, workers' opinions are taken into account and, so, they subscribe decisions made. But the social control of managers and joint-stock markets, where shareholders try to minimize costs and workers to maximize wages, disappears. Besides, the worker has no incentive to save, since he is not proprietor of the future income. Finally, company decisions are less prompt as, in order to obtain information,

more networks are required (see Trincado 1994). However, the way of decision-making is still being debated among non-hierarchical societies. A common technique is formal consensus, including techniques for ensuring that decisions can be made within reasonable timelines and avoiding endless turning around in circles. Various forms of supermajority voting or consensus minus one are also used.

There have not been many real self-managed experiences, but history records their intensity (see Gide 1928). Some examples are the Paris Commune of 1871, the Russian Soviets of 1917, the Italian and Hungarian Factory Councils of 1919-20, or the Spanish Civil War experiences in the republican party from 1936-9. Also Tito's Yugoslavia, the Israeli Kibbutzim, and May 1968, can be cited.

The Spanish experience is quite representative (see Preston 1984). At the end of nineteenth century, anarchism was represented in Spain by the terrorist secret society "the black hand", which dimmed the public image of Anarchism. However, in 1910 the CNT union was created with 2,600,000 members, a massive affiliation. Spanish anarchists' representatives went to Moscow, but in 1922, they refused to adhere to the Third International and to approve the "proletarian dictatorship". The movement, instead of being weakend, created the non-conformist FAI (Federación Anarquista Internacional) in 1927. For the European libertarians, used to seeing the anarchists associations defeated, Spain represented a field of freedom and hope.

It was in the Spanish Civil War (1936-1939) that anarchism could be put to the test. During the first months, it was not the government but the people who offered resistance to the insurrectionist forces of General Franco. Then, satisfactory self-managed experiences were carried out during a short period of time in republican areas.

Anarchist movements tried to eliminate power and property between the workers. Self-management was implemented in very diverse agricultural regions, such as the poor Aragón and Andalusia and rich Levante areas; as well as in the industrial concentration of Catalonia; and Extremadura and Castile. Many authors, such as Leval (1938 & 1975) and Orwell (1986), relate these anarchist self-managed experiences.

During the war, anarchists had to fight against nationalistic forces under the leadership of Durruti. But anarchists also had to fight against Socialists and Communists. The Communists tried to enforce property rights and recover centralism and State authority. They militarized themselves, using arms against anarchist social revolution. This discord has been considered determinant for the republican defeat, as republicans under-provisioned the anarchist Aragonese and Catalan fronts.

There are also present successful experiments in worker control and cooperatives. The Mondragón cooperative movement in the Basque country in Spain is perhaps the most famous. Founded by a priest in search for Judaeo-Christian values (José María Arizmendiarieta), Mondragón began from a single small worker-owned and worker-governed factory. It entails now a network of 150 enterprises - the larger being the supermarket chain *Eroski*, with 23,000 worker-members and customers with their own credit unions (see Whyte & Whyte 1991). As Cheney (1995) explains, in Mondragón each worker is an economic owner of his/her coop through a complex system of investment and return. Often up to 70 percent of profits go to owner-members in the form of individual benefits; 20% is socialized as reinvestment in the coops; and 10% is contributed to community projects. A central bank of their own is crucial to the vitality and autonomy of the system. Other

coops are schools, social-security and health-care system, a research-and-development laboratory and a consulting organization. Each coop practices a complex combination of both direct and representative democracy. The cooperative system is governed at the highest level by a Cooperative Congress, with proportional representation from each coop. One important characteristic of Mondragón is the multiple levels of solidarity within the coops, be it wage solidarity, maintenance of job security, intercooperative socialization of profits and losses or solidarity with the environment.

MacLeod (1997) shows that the original motives of the Mondragón experiment is shared by other communities. In particular some North American groups share its objectives. The success of these experiments demonstrate that in a global village business for people is possible.

### *Time-Based Currencies*

An “objectivist theory of value” is the basis for many anarchist policies. The “labour theory of value”, advanced by Ricardo and Marx, considers the exchange value of commodities as determined by the amount of labour put into obtaining, manufacturing, processing, distributing, and transporting them. In the same vein, the Energy theory of Value is an attempt to make energy output of workers and energy expenditure on goods/services the basis for value in Joules. These theories banish the market system myth of price of a commodity being determined by its marginal utility to the consumer and producer. Marginalism only concentrates on exchange and ignores the reproduction of the conditions of labor and society. It ignores the dynamics of a capitalist economy and the production relations that underlie the market. Orthodox economic theory leaves out class struggle, alienation, hierarchy and bargaining power (see Lum 1890).

Recently, some local currencies have been based on time although participants are not primarily anarchists. In the 1990's, time dollar projects emerged all across the USA. They succeeded in revitalizing several neighbourhoods and in offering older residents activities in exchange for time credits. This is the case with East St Louis, New England, Washington DC or the Member to Member Time Dollar Programme in New York. Besides, the London Time Bank runs in community centres in the UK, the SEL in France or the Wir in Switzerland. Other projects have been developed in Japan and China (see Cahn 2004 & Boyle 1999).

Critics point out that in many of these Time-dollar based currencies, there is no way to ensure that people are not paid more or less than an hour per hour. Also, they ignore factors like value-added work, which incorporates past labour, such as time spent in school. However, many anarchists call for replacing money with new value systems, new exchange paradigms, and new means of production and even for the abolition of money. This last radical proposal is quite controversial: the prevailing argument against it is that the globalized nature of the world makes an economy without currency inconvenient, if not impossible. Nevertheless, an alternative to money could be a gift economy, based on the free distribution of goods and services and advanced by anarcho-communists. They strive for a society without any money and propose, instead, societies based on direct workers control. Anarcho-communists today are involved in various broad labor and community issues; generally revolving around housing, labor struggles/strikes, and building the anarchist movement.

### **Anarchist Law**

Anarchist legality can be said to be a contradiction in terms, as some define

anarchy as communities without law. But in an anarchist society, law continues to exist. The only difference—it is said—is that law would be effective without the need for any authority. In hierarchical societies, an authority normally uses violence, emotional manipulation or propaganda to enforce the law. But anarchist laws would exist only to the extent that they are considered just by the members of the society, and hence obeyed voluntarily. Empirical research on anarchist law is a field of legal studies which is still young and likely to develop rapidly in the future, as more and more non-hierarchical business are created.

Most free market anarchists hold the non-aggression principle against the person or property of another. This mere principle creates conflict between leftist and market anarchists, as many leftist anarchists consider private property ownership to be a form of violence. Leftist anarchists propose legal changes, such as tax exemptions, to encourage worker cooperatives and other egalitarian structures rather than bureaucratic ones (Martin 1999). Support organizations such as the Plunkett Foundation in the UK and international bodies such as the International Cooperative Alliance in Geneva, and the Food and Agriculture Organization in Rome provide guidance to movements and governments willing to encourage cooperatives through regulatory reform. The International Co-operative Alliance has provided technical input in drafting legislation in a number of countries.

From the rightist anarchism, Benjamin Tucker first developed the free-market conception of anarchist law. He defended common law juries. His theory recently influenced Rothbard (1978). Other anarchist legal theorists are David Friedman, Morris and Linda Tannehill, Jarrett Wollstein, Hans Hermann Hoppe and George H. Smith. In this line, Barnett (1998) suggests that an anarchist

legal system will include private insurance agencies with private arbitration as providers of "law enforcement" services. Benson (1991) exemplifies a stateless law society with the customary Kapauku of New Guinea. The Kapauku had no government, yet enjoyed a prosperous existence. Personal protection was provided by kinship groups. Disputes were settled by prominent and wealthy men who followed well-established rituals and memorized precedents. According to Benson, the non-governmental legal system of the Kapauku is similar to that of Anglo-Saxon England. In England, the evolution of state involvement in law had nothing to do with the promotion justice for all, preserving freedom, or protecting citizens. It was concerned with raising money to pay the upkeep of the constant wars waged by British monarchy. Anyway, as the anarchist anthropologist Harold Barclay (1990) points out, an anarchist society could theoretically develop a type of hereditary system. Such arrangements could become the foundation for a caste system. They could eventually evolve into a formal state.

Many anarchists/libertarians believe in the policies of decriminalizing and deregulating drugs. Criminalization has produced violent crime motivated by the need to obtain money to pay artificially inflated price of illegal drugs. Competitive free market in drugs, anarchists say, would produce safer drugs and less needle sharing, i.e., less AIDs transmission (see Miron 1999, 2001, 2003; Basov et al 2001). Other anarchists also defend the freeing up global immigration laws.

### **Anarchism in a Global Age**

In the first quarter of the 20<sup>th</sup> century, anarchist movements achieved relative, short-lived, success in Europe. They were violently repressed by states, as in the case with the Spanish Civil War. After, during the Cold

War, the philosophical influence of Anarchism remained latent. In the 1960s and the 1970s a surge of popular interest in Anarchism occurred. Since the mid-1960s, anarchists have been involved in special in student protest movements (see Farrell 1997).

In 1970's Denmark, Freetown Christiania was created in Copenhagen. This was a partially self-governing city established by a group of hippie squatters in an area of abandoned military barracks. They developed their own set of rules, independent of the Danish government. The housing and employment crisis in most of Western Europe led to the formation of similar communes and squatter movements. In the Netherlands, a former tax office was squatted (De Blauwe Aanslag); in Germany, people from Hamburg squatted empty flats. The phenomenon has become global, affecting also Latin America and others (Nowicki 1999).

Beginning in the later part of the 20<sup>th</sup> century, anarchist primitivists like John Zernan began to proclaim that civilization – not just the state – would need to fall for anarchy to be achieved. Policies proposed by this movement clash with other anarchist proposals. For instance, while for anarcho-syndicalists worker self-management would render social systems fundamentally more humane, for some primitivist authors, notably Bob Black, an anarcho-syndicalist revolution would maintain oppressive work and workplaces. A rejection of industrial technology is also prominent in the views of many Green anarchists. This worldview is associated with the growth of the anti-roads movement in the UK, Earth First in the US, and the actions of Theodore Daczynski (the "Unibomber").

There has long been an association between Anarchism and the arts. Anarchist art seeks liberation of the total human being and the imagination. Actually, surrealism in particular was equated with Anarchism by its founder



Andre Breton. In music, Anarchism has also been associated with the more explicitly political anarcho-punk, and the techno music scene. Like socialism, communism and even fascism, Anarchism has developed a symbolism which has become associated with a variety of groups and movements. It has also been “recuperated” by capitalist industry.

In the later part of the 20<sup>th</sup> century, and the start of the 21<sup>st</sup> century, Anarchism (or anti-authoritarianism) has been seen to have the same influence as Marxism did during the protest movements of the 1960’s. With the uprising of anti-authoritarian movements in the Zapatista communities in Mexico, the people’s uprising starting in 2001 in Argentina, and the global growth of interest in non-statist, anti-capitalist beliefs and organizing have given Anarchism new life within various movements.

Globally, Anarchism has also grown in popularity and influence as part of the anti-war, anti-capitalist and anti-globalization movements. As we said, European Anarchism developed out of the labour movement; but North American Anarchism also takes strong influences from the American Civil Rights Movement and the movement against the Vietnam War. The underlying principles are the same as the ones defended by the demonstrators against Iraq war. Recently, anarchists have been known for their involvement in protests against World Trade Organization, Group of Eight meetings and the World Economic Forum. These protests are generally portrayed in mainstream media coverage as violent riots. Some anarchists are part of the black blocs at these protests (all people within the bloc wear black and cover their faces to avoid police identification). Others are critical of the black bloc because some have engaged in property destruction against multi-national corporations and have thus gotten a label as “violent”.

Networking has led to the success of various large scale anti-war and anti-globalization mobilizations (such as the protests against the WTO Meeting of 1999 in Seattle, and the Bay Area shut-down during the start of the second Iraq war). These recent technological developments have made the anarchists cause easier to advance. Many people use the Internet to form loose communities which could be said to be organized along anarchist lines.

The above-mentioned Earth First movement is a network of various collectives formed along anarchist principles. They engage in direct action and eco-defence, such as tree sitting and ‘locking down’. In the modern anarchist movement, eco-anarchists generally defend animal rights. They believe in deep ecology, which embraces biodiversity and sustainability and critiques modern industrial agro-production (Bookchin, 1982). Private/government exploitation of collective social wealth must be substituted by more ecological community processes. Much of the Green Parties are influenced by anarchist philosophy, the same as Peace Movement. The green anarchists identify “civilization” with repression and destruction (to humans and the environment). Institutions cannot be reformed. We must reconnect with the wild to create meaningful change.

Also, from the right wing anarchism, the Libertarian Party of the USA and other countries fields itself at elections, and tries to influence public opinion.

Anarchism is not constrained to political protest, however. As we have said, anarchists also engage in building parallel structures and organizations, such as organizing around housing, land issues and work, Food Not Bombs, infoshop and radical social centers or new types of schooling systems and media. This is in line with the general anarchist concept of creating “dual-power”, creating the structures for a new anti-authoritarian society

in the shell of the old, hierarchical one. A book analyzing how this new “anarchic” mode of production is possible is Eric S. Raymond’s (2001) *The Cathedral and the Bazaar*. Here are some examples of major groupings of anarchist collectives and groups throughout the world:

- Africa: Southern African Anarchist Federation.
- Europe: Networks of collectives like Food Not Bombs, Indymedia, Reclaim the Streets, Critical Mass, Anti-Racist Action and many more. Large scale anarchist federations like the Anarchist Federation, Class War and anarcho-syndicalist unions. Anarcho-primitivists and eco-anarchists, who played a huge role in the anti-roads movement in the 1990’s. Radical animal liberation and squatting groups are also very strong.
- Asia: While Anarchism once had a large influence in China in the 1900’s and Korea in the 1920’s, Anarchism today in Asia is followed by small amounts of collectives. However, in the Philippines, organized anarchist groups are starting to form. Anarcho-punks and youth make up a large part of this movement.
- New Zealand/Australia: New Zealand has a wide range of anarchist collectives, working on various projects. Australia has small groups of various collectives, and radical infoshops and spaces.
- South America: South America has some large anarchist federations, mostly anarcho-communist. Mexico has various radical infoshops and anarchist establishments, and many anarchist collectives work to support the Zapatista movement.
- North America: Many collectives and anarchist groups exist within the United States. Large scale American anarchist groups include Green Anarchy, NEFAC (North Eastern Federation of Anarcho-Communists), IWW and others. Canada also has members of

NEFAC, and has its own host of anarchist groups and collectives.

## Conclusion

Global age has reinforced anarchist movements. The cutting down of real social relationship between people, the anonymity and a-culturization of market economies, the totalitarian decisions made by nations or the arbitrary “war on terrorism” waged by superpowers, make anarchism still alive. Anarchist movements amount a salutary shock against power structures. Its resurgence shows that Orwellian world will be imposed not without trouble and resistance. The fact is that a somehow non-hierarchical and out of property world exists beneath individual property and power structures. Anarchist theorists only try to demonstrate that the maintainance of this world is possible.

## Internet sites

A People’s Libertarian Index.  
<http://flag.blackened.net/liberty/>  
Recherches sur l’anarchisme.  
<http://raforum.apinc.org>  
Anarchism.net. [www.anarchism.net/](http://www.anarchism.net/)  
HistoriaSiglo. [www.historiasiglo20.org/enlace/s/eng.htm](http://www.historiasiglo20.org/enlace/s/eng.htm)  
Infoshop.org. [www.infoshop.org/](http://www.infoshop.org/)  
Anarchists and Fellow Travellers.  
[www.sniggle.net/anarchism.php](http://www.sniggle.net/anarchism.php)  
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### **Introduction**

The Austrian School of Economics (also known as the “Vienna School”) emerged around one of the pioneers of the 1871 Marginalist Revolution, Carl Menger (1841-1921), at the University of Vienna. Menger, at the same time as William Stanley Jevons and Léon Walras, introduced the two basic marginal principles, decreasing marginal utility and the equimarginal principle. Unlike Jevons and Walras, he avoided all mathematics. Menger founded a “school of thought” which has retained its distinctive character ever since. The distinguishing points of the school are the importance of subjectivism, expectations and uncertainty; the Hayekian cycle, time-defined capital, methodological individualism, alternative cost and, above all, the importance of “market processes”. Members of this group have engaged in numerous debates with other schools of economic thought, such as Keynesians, Marxians and Socialists. They present a general political, economic and philosophical defense of laissez-faire economic policy.

The First Generation of Austrian School scholars included Friedrich von Wieser and Eugen von Böhm-Bawerk. A later generation was dominated by Ludwig von Mises and Friedrich von Hayek. The Austrian School maintained its base in Vienna until the 1930s, when most of its members were exiled to Great Britain and the United States. Then, a Third Generation of the Austrian School emerged, composed of important economists such as Morgenstern, Machlup and Vera C. Smith. The Fourth (American) Generation, including Israel M. Kirzner or Murray N. Rothbard, have demonstrated the push of Austrian School ideas (see Holcombe 1999).

### **The Historical Setting**

Rothbard (1976) argues that the Austrian School of Economics emerged from sixteenth century Spanish scholasticism (see also Huerta de Soto 2002, 249-251). But the first formal stage of the school is based on Menger’s theory. Gustav von Schmoller challenged Menger after the 1871 presentation of his subjective theory of value. The debate on method (*methodenstreit*) divided the German-speaking world: Austria and its universities for the Austrian School, Germany and its universities for the German Historical School (Mises 1969).

Unlike Schmoller and his disciples who defended government in the hands of the professors, the bureaucracy or the Junker aristocracy, Menger was highly critical of the higher Austrian aristocracy (see Moser, 1997). Menger argued that institutions cannot be forced to emerge as they evolve spontaneously. In the market, services rendered are voluntary and create an order resulting from human desires to adapt and survive.

Wieser and Böhm-Bawerk taught at various universities (Vienna, Innsbruck, Prague) and were recurrently appointed to the ministries of finance and commerce in Vienna. Böhm-Bawerk’s performance as Finance Minister remains unclear. Economic historian Alexander Gerschenkron blamed him for Austria’s economic backwardness because he was reluctant to spend on public works projects (Gerschenkron 1977:127-8). But Joseph Schumpeter (1925:79) praised his efforts toward “the financial stability of the country” (see Mises 1969:18). Wieser’s contributions have been subject to debate. He is renowned for his *Social Economics*, but Mises (1978:35-6) claimed that he was “more harmful than useful”, and that he “never really understood the gist of the idea of Subjectivism in the Austrian School of

Thought”.

### **Socialist Calculation**

The early success of the Austrian School came to an end with the collapse of the Austro-Hungarian Empire in 1918. In the new republican atmosphere, many Marxists began to take positions of power. The Austrian School's traditional controversy with Marxists such as Max Adler, Otto Bauer and Rudolf Hilferding changed when several prominent Pareitians accepted an efficient socialist organization of economic society. Their “Socialist Calculation” debate generated other distinctive features of Austrian theory, particularly the theory of knowledge laid out in the seminal contributions by Hayek.

At the end of World War II, Mises presented a theory of the economics of war in *Socialism*. He showed that authoritarian mode of organization does not allocate resources according to their most highly valued use by individuals. Economic calculation is impossible under socialism (Streissler 1988:195). Mises continued this issue in *Nationalökonomie* that he expanded into *Human Action*, which appeared in 1949. This work remains the economic treatise that defines the Austrian School.

In 1935, Hayek edited a book on the ‘socialist calculation debate’. In Hayek (1945), he tried to move the debate forward. He claimed that prices are not merely rates of exchange between goods, but also a mechanism for communicating information. In Hayek (1988), the “fatal conceit” of Oskar Lange and other Socialists had been that they believed order could be “designed” by a planner who gets prices right. They did not realize the limited knowledge constrains, not only of individuals per se but also of planners. Conversely, “spontaneous order” arises from the interaction of a decentralized group of self-seeking agents acting in a price system. Hayek's elaboration on this evolving order is

found in various places. He linked this issue with political and legal theory.

In 1944, in his best-seller *The Road To Serfdom*, Hayek had pointed out that tyranny is the political corollary of socialism, be it Russian Marxism or German nationalist socialism. Hayek enlarged his ideas in 1960 in *The Constitution of Liberty*. Endorsing the famous Humean definition of liberty as the rule of laws and not of men, Hayek shows the legal requirements for maintaining a commonwealth of free citizens. Hayek distinguishes between socialism and the welfare state. Welfare state is compatible with liberty under certain conditions. Conversely, for the more libertarian Mises, even the welfare state transforms the market economy step by step into socialism.

Rothbard was Mises student. His *Man, Economy, and State* (1962) is influenced by *Human Action*, and in some areas only strengthen Mises' views. Rothbard's approach to the Austrian School is based on a natural-rights theory of property and the defence of a capitalist and stateless social order. In a series of studies on government policy, Rothbard established a theoretical framework for examining the effects of intervention in the market.

In the same vein, Austrian School theorists have studied the market reforms of the former soviet republics. In 1991, Richard Ebeling consulted with members of the Russian Parliament in Moscow on free market reform and privatization of the socialist economies (Ebeling 1994). Ebeling lectures widely on the problems of the Global economy and of economic reform and change in the former Soviet Union and Eastern Europe (Ebeling 1996), as well as on economic policy in the United States (Ebeling 1995).

### **Democracy and Cooperation**

Political democracy embodied in representative government is for Austrians the

corollary of the economic democracy of the market. As for Hume, only this system will preserve peace in both domestic and foreign affairs. Presently, Mark Pennington is looking at the implications of 'spontaneous order theories' for deliberative democracy and the 'politics of difference' (see Pennington 2000).

Mises (1960) points out that there is no freedom in "laws of nature". The concept of freedom and its antithesis make sense only in referring to conditions of social cooperation, which is the basis of any really human and civilized existence. Only in a free society, Mises says, has the individual the power to choose between morally praisable and morally reprehensible conduct. He adds that just by establishing a market economy the principle of economic democracy can be realized. It votes every day: to become rich in the market is in itself the outcome of a vote taken. It requires success in best supplying consumers.

Mises made some observations on the Cooperative Movement. For Mises, cooperatives are not a method of world reconstruction. The Cooperative Movement struggled for the elimination entrepreneurs and capitalists altogether as "useless exploiters". But, for Mises, the elimination of the private businessman does not reduce sales costs. On the contrary, it increases them. Cooperatives can not stand the competition of private business without the aid of government special privileges and favoritism. Besides, actual cooperatives are not based on an ideal of direct cooperation. They are big businesses organized in a complicated hierarchy. The competitive market economy can be more democratic than the cooperative organization as it is social cooperation under the division of labor for the production of goods and services consumers want to use (Mises 1990).

As Schweickart (1993) observes, the success of the Mondragon cooperative

complex in the Basque Country indicate that a libertarian socialist economy can flourish. So, Carson (2004) reconciles the Austrian and Marxist anti-statist theories. The end of liberal democracy as a dominant political paradigm, and its replacement with philosophical anarchism and a decentralized and pluralistic political order, would naturally generate a brand new economic paradigm. The result could be an economic order where the worker-oriented enterprise replaces the capitalist corporation as the dominant mode of economic organization (Preston 2003). Moreover, Rothbard (1965) expressed sympathy for many of the criticisms of state capitalism advanced by the classical socialists. However, he attacked them for blaming the market rather than the state for the exploitation inherent in state capitalism and for their effort to achieve socialism by reactionary methods, statism and militarism (see Raimondo 2000).

### **Progress and Development**

The Austrian economists do not derive optimism concerning mankind's future evolution from their epistemological convictions. Some seem to be conservative in a Humean sense. But most of them think that logically indefensible dogmas would eventually be rejected by all reasonable men. They reject the logical relativism implied in the teachings of the Prussian Historical School: there is a body of economic theorems valid for all human action irrespective of time and place. Intellectuals must disseminate a correct grasp of how a market economy operates to teach those blinded by ignorance and emotions. Economic theory is not improved by mathematical equations, however. They are useful where there are constant quantitative relations among unmotivated variables, as in physical phenomena. They are inappropriate in the field of conscious behavior and praxeological



phenomena.

A basic figure like F. A. Hayek (1960) explained 'why I am not a conservative'. For him, conservatism, until the rise of socialism, was the opposite of liberalism. Conservatives are usually protectionists or discredit free enterprise. Conservative distrust of the new is connected with hostility to internationalism. But the decisive objection to conservatism is that, since it does not indicate another direction than current tendencies, it cannot prevent their continuation. Actually, Boettke (2004) argues that Austrian libertarianism can be viewed as an impetus for a progressive research program in political economy that addresses issues of social cooperation in case of conflict.

With regard to development strategies, Austrians claim that the approach to development assistance through government management of the economy has failed. It was based on a theoretical consensus that fractured in the 1989's fall of the Berlin Wall. So, to fill the void, Austrians propose the New Comparative Political Economy. This emerging literature studies how alternative political, legal and cultural arrangements impact on economic performance (Boettke et al 2005).

This theory gives new diagnosis and advices for underdevelopment. For Soto (1989), the causes of underdevelopment are black market, onerous regulations and lack of property rights. In Lima, Peru during the 1980s, hundreds of regulations made it very difficult for an entrepreneur to negotiate the bureaucracy and start of new business. For Soto (2000), turning "dead capital" into "live capital" implies enabling a more secure property rights system. Then, people will be able to realize the benefits of specialization and individual savings will be channeled into capital investment.

Unfortunately, poor countries are particularly prone to the wasteful, prestigious

government 'investment'. Underdevelopment will be solved only by creating a set of credible institutions that constrain predation and make easy individual imaginativeness. However, institutions that are successful in one country can not be exported and imposed in other countries in the hopes that they will stick. Many Austrians economists defend that free trade is the solution for global inequality (Ebeling 1993). Price liberalization, privatization, low inflation, fiscal responsibility, low levels of taxation and regulations, and open international trade constitute the general policy recommendation. The second set of policy questions is associated with the entrepreneurial process and how microeconomic environment impacts in decision making (Boettke 1989, 2003).

We can review some Austrians recommendations for specific poor areas. Alfred Schütz is for Neo-Austrians in US the political and economic scientist who, moreover, could give a new orientation to African political economy (Ki-Zerbo 2001). Robert Wade (1990) analyses the debate about industrial policy in East and Southeast Asia. Rothbard criticized US Middle East policy. In Rothbard (2000), he described the Middle East as very much like Africa in that the existing "nations" are geographical expressions resulting from the arbitrary carving up of the continent by Western imperialism. "Oil wars" are useless: the power of OPEC increasing the price of crude oil, thus injuring the U.S. consumer and economy, is not unlimited. OPEC's revenues would fall as buyers purchase far less oil. Besides, to host dictators, despots, etc. dubbed "pro-West" makes U.S. not credible in the fight against "bad guys". Certainly, the U.S. hatred of Iraq is based on oil, but not for economic reasons. It is based on the most powerful influences on American foreign policy: the long-term "friendship" with the



"pro-West" despots of the Saud family and the influence of the powerful Zionist lobby.

Rothbard says that not even United Nations is a guarantee. UN was originally conceived as a "collective security against aggression." Given existing national boundaries, any "aggression" of one state against another must trigger the nation-states of the world to band together to combat and "punish" the designated aggressor. The effect of this policy is to freezing the unjust status quo in place forever.

Many Austrians criticize also international economic institutions as WTO and IMF. Razeen Sally (1998) shows that a libertarian concept of international policy seeks to create unsubsidized and unmanaged free trade in decentralized political institutions. Wilhelm Röpke (1959) and the Ordoliberal, think possible to be internationalist on trade and isolationist in politics. The smaller the political unit, the closer government will be to the people, which means it will be easier to keep it in check and macroeconomic planning will be less feasible. At the same time, smaller political units are more dependent on trade with their neighbors, helping to build the peace. Röpke opposed all post-war efforts to create a world government. He predicted the World Bank and the IMF would only exacerbate the problems of international debt and world inflation. The IMF is designed to lead governments into regulations and to support a bureaucracy conveying the impression that world trade depends on agreements among governments, not on spontaneous cooperation among producers and consumers. According to Hazlitt (1984), being the problems of balance of payments usually result of domestic disorder, a supergovernmental aid tends to subsidize bad economic policies.

### **Social Policies**

Austrian School's economic proposals are

based on an optimistic sketch of the market. Their social proposals, however, are based on a pessimistic Hobbesian view of the nature of man. So, they defend 'pessimistic' social policies. Mises thought that feminism was a revolt against nature akin to socialism. A woman is simply the lover and mother who serves the sexual drive (Mises 1922). Mises had high praise for British colonialism, and felt it benefited all its subjugated peoples. He assumed the existence of "better races" (see Tucker and Rockwell, 1991) based on a somewhat elitist theory. For him, the masses do not think (Mises 1961:195-6). "The immense majority of common men are both too dull and too indolent to follow and to absorb long chains of reasoning" (Mises 1969:16). Thinkers in a market economy are, of course, entrepreneurs.

Rothbard also believed in the superiority of the elite, and that society is filled with "ineducable masses" (Rothbard 1978:122). Rothbard does not attribute the problems of blacks or other minorities to racism and prejudice, but to parasitic values of idleness and irresponsibility found in those communities (Rothbard 1978:154). Although Rothbard's philosophy led him to an application of property rights dogma, he argued for abortion as if the fetus is an invader of the mother's property: "What the mother is doing in an abortion is causing an unwanted entity within her body to be ejected from it..., as a parasite within or upon some person's body" (Rothbard, 1978: 108). Once the child is born, it cannot be killed or maimed, but it is the property of its parents as long as it lives with them. They can do whatever they please with it, even sell it. "Now if a parent may own his child (within the framework of non- aggression and runaway-freedom), then he may also transfer that ownership to someone else" in "a flourishing free market in children" (Rothbard, 1982: 103).

Austrian School leftist critics affirm that, like libertarians in general, Austrians sometimes favor leftist policies, like opposing censorship, war, and drug prohibition. However, many Austrians have been hostile to liberal constituencies, government interference in the labor market in affirmative action towards women, minorities or workers and environmental regulations. "Civil rights legislation is the worst regulatory intervention in labor markets" (Rockwell, president and founder of the Ludwig von Mises Institute). However, they tend to obliterate drawbacks from the private labor markets. Rockwell defended the Los Angeles Police Department after its beating of Rodney King was caught on videotape. The editor of *Liberty* criticized him, but other noted libertarians, like Murray Rothbard, publicly defended him (Heider 1994:150).

### **Capital, Profit and Trade Cycles**

A principal feature of Austrian School economics compared to Classical Economics is the stress of the element of time and uncertainty in non-Keynesian terms. Business is based upon the anticipation of the future. In a world without change, there would be neither profit nor loss. But in the real uncertain world, retailing adjustment adds value by keeping products ready for use at those places and at those times consumers demand them more urgently. For Austrians, private agents, the same as politicians, make errors. They correct them over a period of time where they discover the "equilibrium" prices at which exchange could satisfy everyone.

So, Austrians have a time-theoretic approach to capital and interest. They base their monetary over-investment theory on the business cycle, unlike Keynesians. Böhm-Bawerk demonstrated that the normal rate of business profit is the interest rate. A growing economy is not just a consequence of

increased capital investment, but also of longer and longer processes of production that makes capital non-homogeneous. Böhm-Bawerk engaged in a prolonged battle with Marxists over the exploitation theory of capital.

Mises presented a broad outline of the Austrian theory of the business cycle in *The Theory of Money and Credit*, drawing on Böhm-Bawerk's theory of the structure of production, the British Currency School and Knut Wicksell's theory of interest rates. Mises showed that an artificially low rate of interest maintained by credit expansion, misallocates capital and makes the production process too time-consuming in relation to the temporal pattern of consumer demand. As time eventually reveals the discrepancy, markets for both capital goods and consumer goods react to undo the misallocation. As Garrison (1996) shows, the Austrian theory of the business cycle emerges from a simple comparison of savings-induced growth, which is sustainable, with a credit-induced boom, which is not. Saving gets us genuine growth; credit expansion gets us boom and bust. A savings-induced decrease in the rate of interest, based on changes in the desire for future, favors investment in more durable over less durable capital. Changing degrees of "capital intensity" are established. Credit-induced decreases in the rate of interest create a disconformity between the preferences of intertemporal spending of income earners and intertemporal consumption/ production decisions that generated that income. The artificially low rate of interest eventually gives way to a "secondary depression", a high real rate of interest, as investors bid against one another for increasingly scarce resources. Mises supported anti-cyclical monetary policies but, writing in the early 1930s, he said that if, over a period of years, capital had been misallocated by an accelerating credit expansion, no policy could avoid a crisis (see

also Hayek 1935).

Both Mises and Haberler dealt with various misunderstandings. The market works. It adjusts production decisions to consumption preferences. But production takes time, and as the economy becomes more capital intensive, the time element becomes more important. Central bank policies aimed at "growing the economy" prevent lenders and borrowers from stabilizing a natural interest rate. Then, the market reallocates resources according to the underlying institutional arrangements and reactions of market participants. Haberler attributes "the more fundamental maladjustments," to "institutional weaknesses and policy mistakes" (Haberler 1976:26). Haberler focused the attention on relative prices that govern the "vertical structure of production".

Haberler was not a doctrinaire follower of Austrian theory, though. He saw the complexity of the Austrian theory as a "serious disadvantage". To allow capital to be a variable rather than a parameter is to change the subject matter—from macroeconomics to the economics of growth. Relief from the complexities of capital theory together with policy implications attractive to politicians gave Keynesianism an advantage over Austrianism.

Austrian and mainstream economists answer differently questions of policy and institutional reform (see Hoover 1988:231-57). Austrians, who see the intertemporal distortion of the capital structure as the more fundamental problem, recommend hard money and decentralized banking to avoid credit-induced booms. Mainstream macroeconomist's recommendations include fiscal and monetary stimulants aimed at maintaining economic expansion, policies criticized by Austrians.

In the Austrian view, cyclical unemployment is, at least initially, a particular kind of structural unemployment.

The central problem today is chronic fiscal imbalance. Monetizing the Treasury's debt eliminates the risk of default (Garrison 1994). As a solution, Vera C. Smith (Lutz) made a systematic critique of central banking system (Smith 1936) and initiated the "free banking" movement. Only by permitting commercial banks to issue their own currency, which circulate in competition, can inflation be avoided. This topic was later taken up by Hayek himself (Hayek 1976). Wage determination is the central economic problem. Hayek compared the wage-price spiral that accompanies a prolonged expansion to a duel between labor unions and the central bank. Rothbard (1985) defended a gold standard to avoid this spiral. He wanted convertibility at home and abroad to prevent the Fed's monetary depredations, which have reduced the dollar's value. The fractional reserve system has created the business cycle. The ultimate guarantor against inflation is a private banking system with private coinage.

### **Entrepreneur**

Finally, the feature of radical "subjectivism" of Austrian theory versus Classical School, in particular, the supremacy of strategic behavior, gives play to Austrian theory of entrepreneur. Oskar Morgenstern 1935's article on the difficulties of perfect foresight was partly based on Austrian leanings, and discussed the greater generality of "strategic behavior" over "Robinson-Crusoe", price-taking behavior. Together, Morgenstern and John von Neumann wrote their 1944 famous treatise on the theory of games, which laid the foundations for game theory and of a theory of choice under uncertainty. They reconciled some trends of Austrianism with mathematics.

As Garrison (1995) says, in the neoclassical world, explanations of economic phenomena consist of applications of cost-benefit calculus and maximization subject to

constraint, a deterministic framework. In the Austrian world, the market process is driven by alertness, or entrepreneurial discovery (Kirzner 1989), which lies outside the cost-benefit calculus. Positing alertness, entrepreneurship is a *sine qua non*.

Austrians criticize Stiglitz and other neoclassical theorists of information for not having been able to integrate their theory with the figure of the entrepreneur, who subjectively perceives information. The markets neoclassical call "imperfect" for Austrians give rise to potential opportunities of entrepreneurial gain (Kirzner 1997:60-85).

According to Austrian Economists, the more policy-relevant questions are presented in terms of comparative institutions. Is entrepreneurial alertness more characteristic of a market-oriented economy? Is it characteristic of a less taxed economy? According to Kirzner, alertness is exercised costlessly, and so any after-tax profits suffices to call it forth. But then, why should costless alertness not be always exercised to the fullest? Shmanske has provided an insightful answer to these riddles by distinguishing between developing the capacity to be alert to profit opportunities and actually exercising the alertness. Cost-benefit analysis applies to the developing but not to the exercising. Shmansk (1994:221) expresses a preference for institutional arrangements that minimize "artificial," or "unnecessary," costs. The capacity for alertness will be greater in a market-oriented, low-tax economy. Shmansk argued that those bold spirits, entrepreneurs, created technical and financial innovations in the face of competition and falling profits and generated irregular economic growth. Schumpeter expanded his theory of entrepreneurship in a wider theory of the development of capitalism. He remains unclassifiable, though.

Due to their description of entrepreneurship, Austrians seem to have no

real theory of the firm. However, their contributions could ultimately lead to an entrepreneurial theory of the firm based on the market process, property rights and the importance of information and tacit knowledge (Foss and Klein 2002). The only condition to have entrepreneurial competition is not to have restrictions at the entry, even in TNCs. According to Rothbard, monopoly is a result of government restrictions. Antitrust laws should be repealed because they suppose a deterministic relationship between the market structure and economic performance. They have been used against innovative organizations (Armentano 1999:Xi). Recently, the dubbed Resource-Based Theory has developed in the area of strategic approach to analyzing the firm (Lewin and Phelan 1999, 2000). In this literature, the concept of rent is key. Ultimately derived from Ricardo, rent in a "Mengerian" (subjectivist) stand is "the amount paid by contract for the use of a more or less ... durable agent ... entrusted by an owner to a borrower for a limited period" (Fetter 1977:371).

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## Caribbean Politics and Policies

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### **Introduction**

The Caribbean comprises a necklace of countries, republics, territories, commonwealths and microstates that encircle the Caribbean Sea in the western hemisphere. Proximity to the United States has been a crucial factor in Caribbean's political history: the Bahamian archipelago is located 50 miles southeast, Cuba 90 miles due south, of the state of Florida. Continuing east past the island of Hispaniola, seat of the republics of Haiti and the Dominican Republic, and then past the commonwealth of Puerto Rico lies the Eastern Caribbean, home to the Organization of Eastern Caribbean States, created in 1981. Five of the organization's nine members are part of the Leeward Islands: Anguilla, the British Virgin Islands, Montserrat, and the two single political entities of Antigua and Barbuda and Saint Kitts and Nevis. The other four belong to the Windward islands: the Commonwealth of Dominica, Grenada, Saint Lucia, and the third political entity of Saint Vincent and the Grenadines. Continuing westward, past the islands of Aruba and the Netherlands Antilles—situated off the coasts of Colombia and Venezuela, respectively—lie the Caribbean republics on the Central American isthmus.

Mintz (1974:xvii-xviii) has enumerated the features that typify the Caribbean region, which can be characterized physically as subtropical lowlands, usually islands, with an insular ecology. The native populations were essentially annihilated shortly after discovery by the European conquerors. The region was defined early on as a sphere of European overseas agricultural capitalism, based primarily on the sugar plantation system that depended on African slaves. As these

societies evolved throughout 400 years of slavery, abolition, and independence, insular social structures grew up that left little encouragement for the development of local community organizations. Thanks to overseas domination and limited access to land, wealth, and political power for the masses of the Africanized population, national class groupings took on a bipolar form. Indeed, skin color was a status marker that became all the more complicated after abolition with the introduction into some colonies of indentured servants. This introduction involved the massive influx of new foreign populations into the lower social structures under conditions of limited economic, social, or political mobility. The main political feature of most Caribbean nations, therefore, is the absence of any national identity that could serve as a goal for mass acculturation and political cohesion. Finally, the colonial ambience in the Caribbean has persisted longer than in any other area outside Western Europe.

### **Colonial Legacy and Beyond**

Ledgister (1998:11–12) asserts that all Caribbean polities have several things in common regardless of which European power ruled them into the post-World War II era. First, the economies were based on plantations that supplied sugar, coffee, rum, and other tropical products to the metropolitan country. Second, governmental institutions dating back to the seventeenth and eighteenth centuries were modeled on those of the metropolitan powers, with legislatures, judiciaries, and bureaucracies imitating the metropolitan country in both form and function. Once slavery was abolished in the mid-nineteenth century, the established political systems were reformed significantly. These reforms included a distinct expansion of the bureaucracy and the emergence of a middle class descended from the formerly



enslaved population. After the introduction of indentured servants from South Asia, Europe, Indonesia, and China into many of the Caribbean colonies, pluralistic societies developed in which the mass of the population was divided into two or more segments based on ethnicity.

Because those in power had similar objectives, the political and economic institutions of slavery and plantations were similar across the region (Mintz 1974:xix). Thus, Caribbean societies, artificially created and manufactured by the extermination of indigenous people and the subsequent waves of imported labor, did not have many characteristics of other colonized territories in Africa, Asia, or South America. For example, there were no traditional native hierarchies of authority as elsewhere in the colonized world; for example, tribal chiefs, village chiefs, monarchies, or aristocracies. Rather, the framework for order and authority in the Caribbean consisted of the European norms imposed by the colonizers (Ledgister 1998:12).

Two historical markers of the twentieth century are salient in the political development of liberal democracy in the Caribbean. The first, the Great Depression of the 1930s, helped politicize the lower classes in response to the high unemployment, low wages, and abysmal working conditions that served to exacerbate the widespread poverty and deprivation. The era was characterized by massive violent working-class protests from which there emerged traditional labor parties and trade unions. A lower middle class comprising state workers and government bureaucrats in the form of civil servants, teachers, policemen, soldiers, and constables was also evolving thanks in part to the presence in the Caribbean of Christian missionaries. The latter provided enough education to qualify the populace for these positions and acculturate them in a way that

served metropolitan interests. Hence, a strong, state-serving bureaucracy evolved from the very population once subjugated by the state, which, almost paradoxically, contributed to the strength of the democratic struggles (Ledgister 1998:15–16).

World War II and its aftermath helped propel the Caribbean colonies toward their bid for independence. France and the Netherlands, having fallen to the Axis powers during the war, were too distracted to suppress the mass revolts that had begun in the 1930s. Britain had already started to carry out reforms during the war, and once the hostilities ceased, colonial national movements everywhere inspired independence in the Caribbean. The U.S., always hostile to foreign presence in the hemisphere, encouraged the departure of European influence and sought to gain a strong position of influence in the area in the face of the Soviet threat (Ledgister 1998:17).

### **U.S. View: ‘Our Own Backyard’**

In 1823, the Monroe Doctrine staked out the Western Hemisphere as a domain of American influence. Since then the U.S. has justified waging war, capturing territory, and using military might to defend multinational corporations against workers demanding decent working and living conditions in the ‘banana republics’ of the Caribbean. Prior to the Civil War, the South looked at the Caribbean basin with a view toward creating an expanded slave empire. Since the war of 1898, when the U.S. seized Cuba and Puerto Rico from the Spanish, military force has been used many times to depose or install patron dictators and make the area safe for commercial interests. Additionally, the area has been the focus of often whimsically named U.S. foreign policy initiatives, such as Teddy Roosevelt’s Big Stick. This policy foray was followed by construction in 1907 of the Panama Canal, referred to by Black

(1988:xvi) as “the cornerstone of US national defense.”

Subsequently, Dollar Diplomacy, the Good Neighbor Policy, Operation Bootstrap, the Alliance for Progress, the Caribbean Basin Initiative, and Operation Ocean Venture, to name a few, all managed to wield enough dominion to keep these small gems powerless and impoverished. Between 1927 and 1933, the U.S. launched its first military invasion of Nicaragua to stave off a guerilla insurgency, only to face a stalemate. Likewise, the 1954 overthrow of Guatemala’s Jacobo Arbenz showed that the U.S. would stop at nothing to forestall any perceived threat to the multinationals it considered one with its own sovereignty. From 60 years of war games on the Puerto Rican Island of Vieques to the 1983 invasion of Grenada, U.S. military intervention and adventurism in the Caribbean have reflected the U.S. view of the Caribbean as its own backyard (Black 1988).

The overall effect of U.S. influence, intervention, and adventurism in the Caribbean has affected Caribbean politics by cultivating conservative political leaders that have sought U.S. sympathy and aid because they were eager to enhance their own power. Such leaders have mimicked democratic rhetoric while exercising brutal authoritarian control over their jurisdictions. Thus, Washington has accorded only a nod and a wink to such long-reigning strong men as Trujillo of the Dominican Republic, the Somozas of Nicaragua, the Duvaliers of Haiti, and Batista of Cuba as long as they spouted the proper rhetoric and allowed so-called free enterprise to flourish. These policies allowed the rich, ruling minority and the impoverished majority that typified colonial times to remain intact. Once these strong men no longer served the U.S. imperative, for whatsoever reason, they were casually disposed of in whichever fashion Washington deemed convenient (Black 1988:xix). It should also be

noted that even democratically elected officials and leaders were not exempt from Washington’s interference, intervention, and even forceful removal. For example, the political history on the island of Hispaniola, home to Haiti and the Dominican Republic, was essentially written by the United States in the twentieth century.

Haiti, formerly Saint-Domingue, was dubbed the *Pearl of the Antilles* in colonial times for the wealth it bestowed on France. Its slave rebellion in the eighteenth century, deeply influenced by the French revolution of 1789, was a complex and dramatic struggle that culminated in 1804 in independence. France decreed liberty for the slaves in 1794 but was loath to respect the colonial constitution written by the French appointed governor Touissant Louverture, which called for self-governance. Bonaparte reestablished the slave trade to Saint-Domingue, captured and murdered the Jeffersonian Touissant, and sent 50,000 French troops to restore slavery. However, these troops, decimated by yellow fever, were defeated at the hands of fierce insurgent troops who swore to die rather than continue to live under France’s sway (Williams 1970:254).

By 1826, land had been redistributed in such a way that the plantation system was effectively restored and the whip of the metropolitan power exchanged for a callous, mulatto, ruling elite (Williams 1970:334). Bolstered by the U.S., which waited 58 years to recognize Haiti as an independent nation, France demanded that Haiti pay 90 million gold francs as reparation to former plantation and slave owners (Aristide: *The Endless Revolution* 2005). By the end of the nineteenth century, an article by Younge (in Shah 2006:4) revealed that 80 percent of Haiti’s national budget was being allocated to service this loan. Thus, the groundwork was laid for Haiti’s continued immiseration.

Since then, a disastrous succession of brutal dictators has marked Haiti's descent into an inferno of economic deprivation and political chaos. It is the poorest country in the Western Hemisphere and the fourth poorest nation in the world. Prior to 1990, Haiti had experienced thirty-three *coup d'états* since its independence. Haiti's notorious dictator, Francois Duvalier, ruled with an iron fist from 1957 until his son, Jean Claude Duvalier, succeeded him in 1971. Haitians have the Duvaliers to thank for institutionalizing the notorious *tontons macoutes* death squads, which efficiently helped the rulers to enforce the tiny nation's downward spiral into crushing poverty, unemployment, illiteracy, poor health, short life expectancy, and ecological devastation. The younger Duvalier faced a revolt in 1983, at which time "Baby Doc" was escorted out of the country in a U.S. Air Force jet. It was at this time that a priest named Father Jean Bertrand Aristide began his political ascent, aided by a sincere populist platform delivered with the rhetoric of a liberation theologian.

Having established the *Lavalas* ("cleansing flood") party, Aristide became the first-ever elected president in December 1990 after defeating the U.S.'s clear choice, leading candidate Mark Bazin, Duvalier's finance minister and a former World Bank official. By 1991, Aristide was advocating higher wages and an end to the *bracero* program with the Dominican Republic, under which Haitians migrate to harvest sugarcane in the Dominican *bateyes* for abysmally low wages and subhuman working and living conditions. The Dominican government was known to pay the Duvalier's millions of U.S. dollars in a collusive agreement that relegated the Haitian cane cutters to a fate worse than slavery. When the Dominicans turned to the U.S. for support in the matter, they found little, although not because the U.S. sympathized with Aristide and the Haitians—

from the beginning, the U.S. opposed Aristide and his policies of labor reforms and other human rights imperatives. Rather, the U.S. failed to help the Dominicans because powerful U.S. agricultural interests now enjoyed protectionist policies that excluded the importation of foreign sugar (Wucker 1999:126–132).

The sugarcane fiasco of the late 1980s and early 1990s also presented political opportunities that the Dominican government could exploit; most particularly, a largely mulatto population with Spanish colonial cultural ties that sets itself apart from Haiti primarily on the basis of race. As Haiti, whose 99 percent black population is the most Africanized in the Caribbean, descended into political chaos, the Dominicans' economic fortunes also fell. The republic's aging president Balaguer capitalized on the issue to scapegoat its many Haitian immigrants for that country's economic woes. Haitians all over the Dominican Republic were arrested and "repatriated," even those that had been in the Dominican Republic for decades, whose papers the Dominican authorities destroyed. In September 1991 speech to the United Nations, Aristide bitterly denounced these blatant human rights violations. As a result, the Dominican government, which even before this embarrassment had not liked Aristide, conspired with former Duvalier cronies and Haiti's elite to remove Aristide from office. They succeeded shortly thereafter (Wucker 1999:133–138).

In this way, the political and economic fortunes of the Dominican Republic and Haiti are inextricably linked. Having suffered its own historic plague of tyrants, the Dominican Republic now enjoys democratic elections that are sometimes, although not always, free of manipulation and fraud. When the poor majority of Dominicans begin to suffer from the institutionalized corruption and flagrant theft by the administration in power, the

Haitians become an easy target for racist baiting and blame. However, as Wucker (1999:14) notes, rather than expressing sympathy for the plight of Haitian cane cutters, the average Dominican blames them for his or her own misery.

The barbaric U.S. puppet Rafael Trujillo (1930–1961) instituted the *bracero* program and with it the policy of shamefully mistreating and exploiting Haitian cane cutters. At the same time, they were used as a political safety valve, targeted for abuse when the boom and bust pattern of the sugar-based Dominican economy became too painful. Trujillo's regime ended in 1961 when he was gunned down; however, in 1965, U.S. marines landed in the Dominican Republic for the second time since they had installed a military government in 1915 and then departed by 1934. The pretense in 1965 was that communists had infiltrated the democratically elected administration of Juan Bosch and that it was necessary to depose that administration. They installed Balaguer, a former Trujillo crony, who managed to stay on the ballots and steal elections as necessary for three decades until 1996. Clearly, democracy, sovereignty, and self-determination in the countries that live in its own backyard do not take precedence over American self-interest.

The political arm of Aristide's opposition, the FRAPH (Front for the Advancement of Progress in Haiti), was composed of former Duvalier operatives responsible for flagrant human rights abuses and largely referred to as "rebels" in the American press. These operatives managed to oust Aristide a second time in 2004 after the U.S. begrudgingly and conditionally restored him to power in Haiti in 1994. As Haiti's elite has been always well connected with Washington, both were always hostile to Aristide. With the support of France, the covert assistance of Dominican operatives, and a U.S. military escort to

physically remove the democratically elected Aristide, Haiti's short flirtation with democracy ended. Following Aristide's departure, Haiti's economy has continued to unravel as it plunges deeper into social chaos and political anarchy.

The Dominican Republic, in which popular elections have taken place regularly since 1996, can boast of a political economy that is slightly less brutish than that of Haiti but rife with misery for the general population. However, the underlying thrust of Dominican political power is the deflection of popular criticism through the engagement of racist demonizing of Haiti and Haitians. Thus, the island of Hispaniola remains in a tragic struggle with itself, the final outcome of which is to ever serve the interests of the colossus to the north.

### **French Influence in the Caribbean**

The grouping that has the strongest political ties to the metropolitan power, the French Caribbean (also known as the French Antilles), consists of the islands of Martinique, Guadeloupe, St. Barthelemy (St. Barts), and St. Martin, a French-Dutch condominium whose southern half belongs to France. St. Barts is unique in that it has never been a plantation economy and today has a predominantly white population. Ensclosed between Suriname and Brazil on the northern coast of South America is French Guiana, the only nonindependent territory on the continent. Martinique and Guadeloupe are overseas *departements* of France and come under French administration, while St. Barts and St. Martin are administered from Guadeloupe. Inhabitants of the French-speaking Caribbean are French citizens, entitled to vote in France's national elections and to unlimited access to medical services on the islands and in France. They use the euro as their national currency, which granted both Martinique and Guadeloupe membership in

the European Union. In 1974, both were also designated as regions, allowing them more local political and economic autonomy. Most affairs other than defense and security are under local control.

Political activity in the French *departements* has a decidedly leftist bent. Indeed, France did not hesitate in 1985 to suppress communist activity when it deployed troops to Guadeloupe after political murders and a series of bombings in the capital city (Schwab 2000:25). The main political parties in Martinique include the Martinique Communist Party, Combat Worker, Martinique Independence Movement, and the Progressive Martinique Party. In the 1995 presidential election, Martinique was the only overseas territory that voted for a socialist candidate. Because the region is looked on as “poor” and is highly subsidized by the French government to compensate for widespread unemployment, its political discourse centers on the island’s economy. In addition, voter participation is low because of voter cynicism about corruption. For example, the 1992 elections were held again in 1994 because of alleged irregularities. Both Martinique and Guadeloupe have small but unpopular independence movements that primarily seek greater local autonomy and not separation from France, because in reality, these *departements* could ill afford to lose their substantial economic support from the mother country.

### **Dutch Influence in the Caribbean**

The Netherlands Antilles is a federation of six islands that are dependent territories within the Kingdom of the Netherlands: the Leeward Islands off the coast of Venezuela (Aruba, Bonaire, and Curacao) and the Windward Islands (St. Maarten, St. Eustatius, and Saba) 500 miles south of Venezuela just east of the U.S. Virgin Islands. The federation members were granted full autonomy in internal affairs

in 1954, and like the French Caribbean, Curacao and Aruba are members of the EU and can adopt its legislation. According to Martis (2003:240), they also have a health care system that covers the vast majority of citizens and is considered decent overall. However, the economies of Aruba and Curacao, unlike those of their French Caribbean counterparts, have enjoyed prosperity not as a result of transfer payments from its former colonial power but thanks to development of its oil refining industry after the 1914 discovery of oil in Venezuela

Nonetheless, having seceded in 1986 to become a separate autonomous member of the Netherlands Antilles, Aruba has a separate status. Following its development of petroleum refining and a successful tourism industry, economic prosperity brought a strong outcry for independence, which became the focal point, to varying degrees, of political parties in Aruba. For example, parties such as the Arubaanse Volks Partij (AVP), the Union Nacionalista Arubano (UNA), and the PPA (Partido Patriotico Arubano) governed the island with a view toward gaining greater local autonomy while maintaining a high economic standard of living. Internal political struggles were a natural part of the process, but when Shell Curacao curtailed its oil refining activities in 1985 because of the global oil glut, the economies of both these islands suffered. Consequently, in 1990, the movement toward full independence was aborted in anticipation of a late twentieth century regional trend away from independence.

Contemporary Curacao, once the main slave distribution center of the Dutch West Indies Company, is described by Martis (2003:229–232) as an ethnically pluralistic, multiracial, and relatively harmonious region of white Europeans, Jews, Arab, Caribbean, Chinese, Indian, and Surinamese. Many citizens from other parts of the Caribbean

migrate to work in the more prosperous islands of the Netherlands Antilles, with Suriname being an interesting case in point because it too was a Dutch colony. Suriname, wedged almost precipitously between the two Guyanas, was granted independence from the European Netherlands in 1975.

Until 1863, Suriname was a slave society similar in structure to those held by other European powers but was reputed to have suffered under an even harsher form of slavery than found elsewhere. Moreover, from the 1930s onward, the lower classes engaged in no autonomous political activism nor did they produce leaders. Hence, there were no demands for better working conditions, higher wages, democracy or responsible government, which had severe consequences for political development. Politics became mired in ethnicity, led by self-aggrandizing political hopefuls of the middle class. Indeed, as Ledgister (1998:136) notes, political parties formed in the 1940s were concerned solely with the interests of the elite classes and represented a plethora of ethnic interests. Whereas Trinidad and Tobago have 12 parties and Jamaica four, Suriname has 29 parties—four Indonesian based, three representing East Indians, two each representing creoles and maroons, and one each representing Moslems and Hindus. Such parties were formed under the “progressive” banner to contest elections or break away from the original parties formed some years earlier (Ledgister 1998:195–197).

Hence, in Suriname, there has never been a shared national vision; rather, in 1980, the civilian government was replaced by a military regime that declared Suriname a socialist republic. This regime continued to rule until 1987 when international pressure forced democratic elections, only for the new incumbents to be overthrown by the military again in 1989. In 1991, a democratically elected government once again returned to

power, but Suriname remains an ethnically fractured society with a negative net migration ratio and a lackluster economy whose per capita income is a fraction of that of the other Dutch territories. Thus, ethnic division, a history devoid of democratic struggles, fractious politics, and poor economic performance come together to the great disadvantage of Suriname.

### **Caribbean Cohesion, Integration, and Community**

Even though a shared history implies similarities in the Caribbean political economy, there is currently very little political cohesion among the numerous polities that make up the region. Nonetheless, agreements and conferences on market integration, confederations, and associations attempt to divine a shared regional purpose and bestow some countervailing power to these tiny entities, which are still plagued by poverty, largely inadequate health care, education and welfare services, and underemployment of resources. Individually, the islands and nations have little control over their international political destiny, which is why various attempts have been made at regional integration, and various institutions jointly established to provide a framework for coordination and cohesion.

The earliest of these arrangements was the Federation of the West Indies. Established in 1947, it was an attempt by Britain to organize the British Caribbean into a West Indian federal state. However, from the very beginning, the former British colonies of Guyana (formerly British Guiana) and Belize (formerly British Honduras) were excluded. Moreover, the federation, ultimately designed to serve the purposes of the colonial legislatures, was too weak to overcome the individual machinations of self-interested and insular island politics. As Ledgister (1998:51–52) pointedly notes, neither Manley of

Jamaica nor Williams of Trinidad was willing to hold federal office for fear that the agency of their own fledgling nations would be subordinated to federal interests. In 1961, Jamaica seceded from the federation and disintegrated shortly thereafter.

A more recent coalition, the Caribbean Community (CARICOM), is aimed at developing leadership, sustainable community, and a better quality of life among its 15 members and 5 associates. CARICOM also aspires to the development of a single market economy, a goal toward which various members have taken steps with regard to tariffs, free movement of goods and services, and freer migration of the citizens of certain community members. Likewise, the Association of Caribbean States was established in 1994 to promote consultation, cooperation, and concerted action, and to strengthen regional integration among its 25 member states and three associates. Among the association's concerns are trade liberalization, transportation, sustainable tourism, and natural disasters. The Eastern Caribbean Central Bank is the monetary authority for eight of the Eastern Caribbean States, providing financial unity through the use a single common currency—the Eastern Caribbean dollar (ECD), a common pool of foreign exchange reserves, and a stable regional monetary policy. Similarly, the Organization of Eastern Caribbean States (OECS) was established to promote unity and solidarity among its members and cooperation toward economic development goals. All members and associate members had achieved their independence from Britain by the 1970s. Not surprisingly, the members hope to promote unity and solidarity through this and other associations to compensate for their small size.

These organizations, the Eastern Caribbean in particular, seemingly endow an overarching sense of unity and integrated

purpose to member nations. However, despite lofty but vague mission statements that call for regional economic growth and prosperity, in the global climate of market liberalization, they are configured to serve the purposes of multinational corporations and not working people. Indeed, evidence on the North American Free Trade Agreement (NAFTA) has indicated that without explicit protections for the environment, wages, and working conditions, workers suffer as a result of market integration and liberalization. Those nations also suffer common political problems, as well as differences in the way local governance is viewed and administered.

### **British Political Heritage of Liberal Democracy**

Because the Anglophone states of the British Caribbean inherited the system of liberal democracy espoused by Whitehall and Westminster, the countries of the OECS are parliamentary democracies within the British Commonwealth. The chief of state is the Queen of England, who is represented in each state by a governor general. Originally established to serve the interests of the mercantile/planter class, and later the entrepreneurial class, this system evolved in both form and style after the various uprisings in the 1930s. It should be noted, however, that wherever mass revolts occurred in the 1930s, the response of the political system was to become more liberal, democratic, and inclusionary even before independence was granted. Thus, the mechanisms were in place to allow for continued incorporation of popular interest in the decisions and activities of central government post independence.

Such liberal democracies are characterized by free and fair elections, competitive parties, and limited government. Whereas there have been periodic changes in the ruling party for certain states, others have seen the entrenchment of a particular party and the

reelection of the head of state for consecutive decades. Nevertheless, the features of liberal democracy, such as free speech, characterized in part by a reasonably fair media; free association, which would include interest group activity; decent standards of public behavior; and a fair degree of civil society participation are current characteristics of many Caribbean states. It is a critical question, however, whether or not the leaders of government and its institutions continue to enjoy legitimacy even in the face of socioeconomic problems such as pervasive poverty, rising numbers of youth gangs, and the consequences of market liberalization and international crime.

The political parties that emerged during the post-1930 period vied for control of the state apparatus, including the significant civil service bureaucracy. Out of this bureaucratic apparatus emerged two important elements of Caribbean politics: authoritarianism and political patronage dispensed systematically by the party currently in power through appointments to the civil service. As regards the authoritarian elements, civil servants, soldiers, and policemen not only served to maintain the social order of domestic safety and civil society but stood ready should the need arise to discipline the masses to serve the interests of the ruling class derived from colonial power. The survival of the second element of political patronage, however, is seriously threatened in the early twenty-first century by economic decline, syndicated crime, and global instability (Payne 1995). Thus, whereas political patronage has traditionally maintained strong political parties and provided a bridge to a political career for the young and ambitious, public sector cutbacks and persistent political problems have shaken public confidence in the system and discouraged talented future politicians. Duncan (2000) points out that the local government systems in the Eastern

Caribbean are inadequately developed and facing significant threats. These include progressive loss of jobs in manufacturing, agriculture and the service sector, notably tourism and off-shore financial services. Global economic uncertainty has resulted in declining national income, trade deficits and increasing external debt service payments. The decline in the quality of social services has been marked by a decline in civility, voter disaffection and cynicism.

The judicial system is in crisis thanks to the existence of large criminal and civil case backlogs ranging from narcotics and drug trafficking to debt collection. Coupled with the inefficient state of court reporting, the judiciary can hardly meet the cost of maintaining itself. Compounding these problems is a dramatic decline in the standard of parliamentary behavior, the withering away of civil discourse, and political anarchy in the inner cities (Duncan 2000:4).

Other threats to community and local governance are the rapid growth in the presence of nongovernmental organizations (NGOs) and multilateral institutions like the World Bank, IMF, and WTO. In fact, the regional groups mentioned earlier could themselves serve to dilute the local power of citizens. NGOs, particularly, are a mixed blessing because they play a critical role in all social sectors of the Eastern Caribbean states and are especially active in women's health and human rights advocacy all across the Caribbean. Among the most prominent, PROFAMILIA (International Planned Parenthood Federation), WAND (Women and Development), DAWN (Developing Alternative for Women Now), CEDAW (Convention on the Elimination of all Forms of Discrimination Against Women), and MUDHA (The Movement of Dominico-Haitian Women) are but a handful of



examples given by Kalny (2003:4–5). These organizations represent activism for women's political rights ranging from family planning, AIDS crisis and treatment, violence and trafficking, economic development, and unionization of the Dominican and Haitian women living and working in the abject conditions of the sugarcane plantations. Nonetheless, despite the critical role played by NGOs in the region, they cannot be considered a substitute for local government because they are incapable of addressing the pervasive poverty and dispossession that characterize Caribbean nations.

Barbados, the most easterly of the Windward Islands in the Organization of Eastern Caribbean States, presents an interesting case of the British influence on Caribbean governance. An appointed Governor General represents the chief of state, Queen Elizabeth II of England. The heads of government are the Prime Minister and a Deputy Prime Minister. General elections, held a minimum of every five years, are called when the Prime Minister dissolves the current Parliament. Voters, who enjoy universal suffrage, vote to elect one Member of Parliament for each of the 30 constituencies to the House of Assembly. Each party nominates one candidate for each constituency, and the party that wins the most constituencies is asked by the Governor General to form the government. The leader of the winning party becomes the Prime Minister, while the party with the second highest number of seats in the House of Assembly is called the official opposition.

Duncan (2000:6–7) notes that the strong tradition of local governance once present in Barbados was abolished in 1967. The central government felt threatened by the power that local councils exercised independent of its control. Services previously provided by local government were transferred to central government ministries. Subsequently, despite

much discussion about reintroducing local government, no formal effort has been made to do so. Instead, voluntary bodies called community councils have been created in all 11 administrative divisions. Nevertheless, the political parties, leaders, and political pressure groups are active and vital within the country. The Barbados Labor Party, the Democratic Labor Party, and the National Democratic Party can best be described as moderate with no major ideological differences. Even though election and political disputes often reportedly have strong personal overtones, they do not have the history of violence that has plagued other Caribbean nations like Jamaica since the 1960s.

The Barbados Labor Party is a member of the Socialist International, an organization concerned with peace, justice, democracy, solidarity, and human rights and adheres to democratic socialist principles that originate in popular labor movements. As the dominant party on the threshold of the millennium, the BLP has, for example, successfully advocated for the reduction of the personal income tax. It has also supported consumers wishing to enforce warranties and guarantees and rights of redress against manufacturers, and has worked to make anticompetitive practices illegal so that businesses may better compete in a fair domestic market. Thus, the BLP is a fairly mainstream, left of center political party that advocates both business and consumer interests but grounds itself in social democratic principles.

The Democratic Labor Party's orientation is somewhat difficult to distinguish from that of the BLP, except that it chooses different rhetoric and is not affiliated with the Socialist International. Its agenda is geared toward the socioeconomic issues faced by Barbados. While in office, the DLP has advocated equal pay for women and legislated in favor of maternity leave, as well as protection in cases

of domestic violence and sexual offences. The party's proposed poverty eradication program addresses homelessness, microloans, subsidies for schoolbooks and uniforms, and other issues of concern to the poor. Other independent parties and pressure groups—such as the National Democratic Party, the Barbados Workers' Union, the People's Progressive Movement, and others—enliven the political debate even if local community politics does not enjoy a strong, official presence.

The politics and policies of Barbados take place within the context of an economy that, despite the usual structure of wealthy minority and working poor majority, has not fared as badly as in some other Caribbean nations. Because 90 percent of Barbadians are black, with only 6 percent making up an ethnic minority of Asian and mixed background, political parties do not seem divided along the lines of racial enmity, distrust, and competition. According to the United Nations Human Development Report (2006), Barbados ranks high among LDCs in human development indicators (see also Kalny 2003:34). It also boasts a literacy rate that is one of the highest in the world and enjoys a diversified economy that presents more career opportunities than in many other Caribbean nations. Telecommunications technology allows many multinational corporations (MNC) to employ Barbadians as data entry clerks and affords the MNCs the ability to transfer this activity around the globe to wherever it can be performed well and at low cost. Other information processing activities have included airline ticket sales, telemarketing, payroll accounting, computer-aided design (CAD), database and software development, and more. Given the nature of the global economy, these jobs have unfortunately been migrating to countries in Asia, where skill levels are commensurate but the labor is even cheaper (Zoll 2003:36).

These seemingly uncontrollable global imperatives hint at the political problems Barbados faces, problems that are easy to overlook given a decent set of socioeconomic indicators like the moderately high per capita GDP. However, without a vibrant and active local government, it is difficult to exert grass roots control over issues that affect health, education, welfare, employment, the environment and social development in general.

In many cases, colonial rule has left the Caribbean with societies so fragmented by race and class that a national identity and shared vision has become difficult to discern. Indeed, some Caribbean nations have been tragically unable to coalesce around a national identity because of racist splintering. These nations—which include Guyana and Suriname—find themselves at the mercy of the worst of underdevelopment. Poverty, conflict, violence, and continuing immiseration seem to be their self-perpetuating lot. Duncan (2000:5) blames this absence of a national consensus—one around a shared vision of a renewed society based on nationalism, sovereignty, independence, and self-sufficiency—for the degree of potential ungovernability in parts of the Caribbean. One such nation is the Republic of Guyana, formerly British Guyana, which is located on the northeastern coast of South America, sandwiched between Venezuela and Suriname.

Economic conditions in Guyana foreshadow the political nightmare. Per capita GDP is a fraction of its Barbadian counterpart. The country struggles with a severely deteriorated infrastructure, potable water is in short supply, roads are too few and in disrepair, farming is hampered by an inadequate drainage and irrigation system, and the power grid is outdated and insufficient, causing frequent blackouts. Expansion of telecommunications service has

also been slower than expected (Country Commercial Guide 1999). Additionally, because it carries a heavy external debt, Guyana has been designated a highly indebted poor country (HIPC) and accorded conditionality agreements. These latter, however, have resulted in the reduction of its external debt and no reduction in the size of its debt service payments. The rate of growth of GDP was negative in 2000, 2003, and 2005 while becoming wildly positive in 2006, perhaps due to a nearly 74 percent increase in intraregional trade from 2004 to 2006 (CARICOM). At present, Guyana is an independent republic within the British Commonwealth and not part of the OECS. Nevertheless, the state does enjoy universal suffrage to elect its chief of state, the President, who is elected by the majority party in the National Assembly through legislative electives held at least every five years. The President then appoints the Prime Minister. Since independence was granted in 1966, elections have been rife with conflict, violence, corruption, and fraud because racism has become politically institutionalized in Guyana.

The ethnic mix in Guyana is roughly 50 percent East Indian, 36 percent black, 7 percent Amerindian, and 7 percent white, including Portuguese, Chinese, and mixed. When slavery was abolished in 1838, Africans no longer wished to work on the plantations and the colonial power had to find other sources of labor in the form of indentured servants from India and other parts of Asia. The country was thus transformed into a racially and ethnically diverse society. Gibson (2003:11–13) posits that colonial economic and population policies encouraged hostility and suspicion among the ethnic groups, thereby preventing the formation of a stable and integrated relationship among them. Indentured servants migrated to the country with the expectation of becoming

wealthy; former African slaves felt they had been cheated of what had been rightfully theirs, especially in the cases when some of their land was appropriated by the government and given to the immigrants.

There are more than a dozen political parties and pressure groups altogether, but the two parties of note are the People's Progressive Party (PPP), supported by Indo-Guyanese, the ethnic majority, and the People's National Congress (PNC), supported by African Guyanese. The PPP has used anti-imperialist rhetoric since its inception and has been perceived by the U.S. and Britain as having communist leanings. Because the British did not want to grant independence to such a party in power, even though it had majority support, Britain and the U.S. devised an elaborate if rather unsubtle scheme of proportional representation to ensure the PNC's victory. Since this party's ascension to power and the granting of independence, two tragic patterns of political behavior have created a downward spiral for this small republic (Gibson 2003:23–53). First, a series of constitutional changes by the PNC's President-elect amounted to little more than a seizure of power, transforming the office into a virtual dictatorship. Election fraud to ensure the PNC's continuing dominance became the order of the day for almost 20 years. Such domination enabled the ruling party to exercise control and exact revenge against the Indo-Guyanese and other ethnic groups, many of whom fled the country in the late 1960s and 70s.

The second political tragedy noted by Gibson (2003) is that the opposition party, the PPP, in an ongoing attempt to destabilize the country, began a campaign of noncooperation with the government. This quest for power and hatred of the ruling party, which included engagement in strikes, boycotts, and sabotage, was directly responsible for the country's economic decline over four decades. Those

who struggled against the authoritarian rule of the PNC were tortured, murdered, and harassed by the police, who engaged regularly in extrajudicial executions. The PPP finally acquired political power in 1992 after a short interlude of a nonracist government whose President succeeded the former president-cum-dictator upon his death in 1985. This leader freed the press, encouraged the judicial process, and implemented policy changes that favored the Indo-Guyanese. However, when free and fair elections were held in 1992, the PPP again came to power.

Upon acquiring office, the PPP reversed many of the policies, programs, and enterprises that the PNC had put into place. They also exacted revenge not only for the years of British colonial domination but for the 28 years of African domination. The extrajudicial killings, now of African-Guyanese residents, continue today. Seizure of African lands, destruction and expropriation of profitable enterprises and organizations instituted by the PNC, corruption in banking, and nepotism at all levels of government employment and contracting has been the order of the day since the PPP's ascendancy to power (Gibson 2003).

Nonetheless, even though Guyana does indeed seem ungovernable, it is not possible to conclude that responsibility for the present day situation can be laid only at the doorstep of racial and ethnic diversity. Trinidad and Tobago, the southernmost island in the eastern Caribbean archipelago, just northeast of Venezuela between the Caribbean Sea and the North Atlantic, has an ethnic mix that resembles that of Guyana but is one of the most prosperous islands in the whole of the Caribbean thanks to petroleum production and natural gas processing. East Indians, originally indentured servants, comprise approximately 40 percent of the population;

blacks make up about 39 percent; and mixed, white, and Chinese the other 21 percent.

Trinidad-Tobago is an independent republic with a parliamentary democracy whose chief of state, the President, is elected by an electoral college for a five-year term. Without doubt, Trinidad is an ethnically divided society: one ethnic party is in control, the other in opposition. Yet the sociopolitical outcome has been very different. According to Ledgister (1998:119), systematic oppression and acts of physical genocide have never characterized ethnic dominance. Rather, political ascendancy and dominance have been executed mostly through free and fair elections within a democratic framework.

Since its inception in 1956, the dominant political party, the People's National Movement (PNM), has fostered nationalism as its policy. Nonetheless, even though the PNM has represented itself as multiracial, it relies on the faithful support of blacks and creoles. For 30 years after the granting of independence in 1962, the PNM imposed a systematic policy of ethnic preferences against East Indians that led inevitably to the development of opposition parties. However, Trinidad, not without its democratic challenges and incipient violence, did enshrine in its constitution protection for those out of power, which explains why ethnic peace has been maintained throughout postwar history. The government has sustained its legitimacy because lower-class East Indians were committed to the political process while those of African descent recognized the system's racial appeal thanks to the use of government patronage as the post-independence state sector grew (Ledgister 1998:120–121).

In Trinidad, the lower classes were politicized as a result of activism and revolt during the Great Depression. Hence, the major parties are based on class alliances and provide a socially important means for

protecting the lower classes from the upper classes once widely associated with the former colonial power. Thus, despite ethnic segmentation, Trinidadian politics is made cohesive by a two-way alliance that helps sustain its own particular configuration of liberal authoritarian democracy (Ledgister 1998:123–126).

### **U.S. Influence Revisited: The Move to the Right**

During the era of bipolar U.S.-Soviet relations, the U.S. often interpreted nationalistic imperatives in its “own backyard” as communist threats, much as it interprets opponents as terrorists today. Most particularly, even though it colluded in Batista’s overthrow and hence Castro’s ascent, the U.S. was blindsided by Castro’s embrace of socialism (Black 1988:58-60). Since then (1959), the U.S. has directed countless coup attempts and unsuccessful invasions at the nation, and ultimately imposed a trade embargo that has crippled the Cuban economy for decades. It was been interpreted by Schwab (2000) as the ultimate wielding of the “big stick,” constituting a human rights violation that has caused decades of harm to Cuban citizens. The fear of another Cuba in the Caribbean has driven interventionist US policy almost to the point of obsession (Black 1988:xvi–xvii).

Indeed, the cold war era in the Western Hemisphere has been characterized by covert U.S. efforts to isolate, destabilize, and contain Cuba through escalated military efforts in the 1980s that turned the Eastern Caribbean states into a maritime police force. Specifically, from 1980 to 1986, military aid to the region increased from \$200,000 to \$20,000,000, much of which was used to support a regional security pact (Regional Security Systems, RSS) and to construct military bases. The RSS was the vehicle by which the Reagan administration undertook the 1983 invasion of

Grenada and later that of Nicaragua. These activities shifted Eastern Caribbean politics sharply to the right as many leaders embraced the U.S.’s anti-Cuban policies and cut off all trading relationships with the communist island in hopes of receiving aid and help from Washington with economic policies that would help them survive. This dependence not only ensures perpetual American influence and keeps Eastern Caribbean leaders at the mercy of the U.S., but, since poverty, geographic location, economic dependence, and uncertainty limit these leaders’ own autonomy, creates a profitable climate for direct foreign investment (Schwab 2000:23–32)

The Caribbean Basin Initiative (CBI), devised by the Reagan administration in 1982, provided a redundant, and therefore useless, 12-year duty free agreement for Caribbean imports, a 10 percent tax credit that never actually succeeded in increasing the volume of U.S. investment in the area, and an aid package of \$350 million to be divided among designated islands. In reality, the region was in need of far more aid, and it is widely agreed that the only tangible subsidy was in the form of a military build-up, primarily in Jamaica, to suppress Grenada’s communist insurgency. As it vied for U.S. favor and hoped to avoid disapproval and punishment, the indigenous leadership swung to the right. However, the economic payoff to the region was more of the same: economic stagnation, unemployment and underemployment, substandard housing, a dwarfed manufacturing and industry sector, and development of the unsustainable and ultimately unprofitable (except to foreign investors) tourist industry. Locked into the role of client state for the U.S., the Caribbean nations and their leadership faced loss of sovereignty, mounting debt, and the crush of market liberalization to their own weak industries (Schwab 2000:35–47).

## **Whither Cuba?**

Since the 1989 break-up of the Soviet Union, Cuba has had to make its way in the global economy by allowing in direct foreign investment from the EU, Canada, and Australia that is eager to tap into a virgin market on which the U.S. has left no footprint since the 1950s. The Cuban government is a 51 percent partner in most major enterprises, which means that foreigners are actually investing in an island-wide monopoly. Without competition, the business climate is safe and predictable. Indeed, it is reported that the billboards in Cuba, once renowned for their revolutionary slogans, have recently begun to convey a consumerist message. The government has been astute about branding and creating corporate style logos for its own state-run businesses and is even planning to launch restaurants in Brazil, China, France, Italy, Mexico, and Spain that serve Cuban cuisine. However, after centuries of colonial domination and decades of authoritarian rule, it is interesting to ponder how far the market-communist marriage can go (Niman 2002).

Post-revolutionary Cuba boasts of the exemplary educational and health care systems it makes available to all its citizens. Indeed, the eradication of income inequality has been the jewel in Castro's revolutionary crown. As Alfonso (2001) points out, between 1960 and 1990 economic stratification declined as the result of a deliberate policy of social leveling. The result was a paternalistic relationship between a powerful state and a naïve society. However, once crisis-driven economic reforms were instituted in the 1990s, social equalization began to disintegrate, and the island nation's efforts to integrate itself into the global economy have been fraught with political pitfalls. Most prominent among these has been the state's unwillingness to change any political and economic structures not directly related to the

global economy. This reluctance is felt most keenly at the level of local government which, from the 1970s until recently, has played an important participatory but not leadership role in bringing about the state's revolutionary goals. That is, local government has served the purpose of implementing centrally planned development policies and ensuring social and regional equity. However, as linkages with the former Soviet Union evaporated and new ones expanded into the global capitalist market, the outcome has been unequal development, with some areas prospering and others contracting. Within this framework, municipalities remain subordinate to the traditional central planning system with no access to the market and no way to increase their income or decide how to spend resources.

After 1989, the U.S. no longer regarded many Caribbean countries as vital to American interest. Therefore, these nations and their leadership found themselves on their own both financially and militarily and under great pressure. For instance, the U.S. extended the embargo that curtailed economic contact with Cuba, thereby inhibiting further Eastern Caribbean trade with Cuba, and cut aid to the region. In dire straits, the Caribbean leaders had no one else to turn to now that the Soviet Union was gone. Yet, even though the Caribbean countries provide a haven for money laundering, drug smuggling, narcotics trafficking, and even the trafficking of women, the U.S. clamped the screws of fiscal conservatism tightly even while implicitly threatening any attempt to integrate Cuba into the region (Schwab 2000).

Given Castro's age, infirmity and impending demise, people are preparing for change in Cuba. In this climate, concerns that the island will revert to its pre-1959 condition as an impoverished, corrupt playground for wealthy Americans are balanced by the island's institutional evolution. Moreover,

the robust educational and health care systems, complemented by a growing cultural pride as the arts and music have flowered, should stand Cubans in good stead during the inevitable reorganization of life after Castro (Cuba after Castro 2006).

### **Economic Transformation: The Tourism Trap**

Seen as a tropical paradise, the Caribbean is an ideal tourist destination. In fact, the tourism model was regarded as *the* vehicle for transforming the former plantation economies into a tool that would lift Caribbean peoples out of their poverty and into development. Hence, as Patullo (2005:17–18) indicates, the region is more dependent on tourism than any other region in the world, with tourism receipts being 25 percent of exports and accounting for more than half the 2000 GDP for four Caribbean states. Nonetheless, colonial patterns of external dependency persist in the form of mostly U.S. ownership of hotels and resorts and domination by foreign airline carriers and tour operators. Employment in the region not only depends on tourism but underscores the dearth of alternative employment. Moreover, the growth of the tourist industry has led visibly to environmental degradation from improper sewerage treatment, sand mining, and careless construction; which have resulted in coastal erosion and destruction of the coral reef, sea grass meadows, swamps, salt ponds, and wildlife habitat and nesting grounds. The Caribbean coral reef, particularly, has suffered damage from cruise ships that also dump up to 2 kg of waste per day, including plastics, oil, and hazardous chemicals (Patullo 2005:137). Sex tourism, the consequent proliferation of HIV/AIDS, and locals supplying tourists with their holiday highs in the form of illegal drugs have further contributed to cultural degradation and social decay (107–115).

### **Conclusion: Future Prospects for a Caribbean on the Move**

The future of the diverse, richly pluralistic, seemingly durable Caribbean states is by no means assured. The needs of U.S. multinationals and the demands of globalization, with all of its implications for resource flows, domestic industry, and international and local political affiliations, combined with the frightening specter of international crime, will steer the region toward an uncertain and shaky future.

Also unsure is an end to poverty and racial/ethnic conflict. Continued growth in relatively prosperous nations like Aruba, Barbados, and Trinidad, to name a few, is uncertain thanks to a ruthless neoliberal agenda and vagaries of global capital that cannot be overridden by even the strongest local political activism. Rather, capital intensive development in labor intensive societies has resulted in the Caribbean being a net exporter of people for 150 years. Governments have always treated migration as a safety valve to rid their countries of some of the chronically unemployed. They also rely heavily on the foreign remittances received to partially offset chronic trade deficits and external debt service payments. Indeed, in their analysis, Abassi and Lutjens (in Ho 2002) point to Caribbean migration as a drawback to development because Caribbean social arrangements have been disrupted to the point at which the economic support of families is in serious jeopardy. Not surprisingly, Haiti is the largest exporter of migrants, most of whom end up in the Dominican Republic, which, in 1999, sheltered approximately 4,000 legally authorized Haitians but an estimated 500,000–700,000 undocumented migrants (Ferguson 2003:8). Likewise, the pull for Haitian migration in the French Antilles is strong: not only common cultural and

linguistic ties, but also the willingness of the tourist, construction, landscaping, and domestic service sectors to hire them (25–26). Dominican migration is also significant because of the push of poverty, malnutrition, income inequality, and limited access to basic services for the poor. Whereas the prized destination is the U.S., Ferguson notes that Dominicans also migrate to Spain, the Netherlands, and Argentina, the latter two associated with a significant illegal influx of Dominican women for the alleged purpose of illicit trafficking and prostitution. The most common means of getting to the U.S. is through Puerto Rico because it is a free associated state and Puerto Ricans are U.S. citizens. In fact, illegal entry into the U.S. is easier from Puerto Rico than from any other Caribbean nation, making Puerto Rico the obvious destination for all those wishing to gain access to the U.S. Puerto Rico itself also hosts a fast-growing immigrant population, including large migrant Dominican communities. However, undocumented migrants to Puerto Rico face no access to services and possible deportation (27). Hence, migration may present a personal economic and social opportunity for individuals and families to improve their lot, but it undermines any political challenge to post-colonial political systems through class-based activism.

Development policies that have favored the needs of U.S. multinationals have also undermined local industry. For example, the imposition by the IMF of neoliberal policies that call for Jamaica to increase its imports has virtually destroyed local dairy, poultry, and agricultural industries (*Life and Debt* 2001). At the same time, the tourist industry throughout the region has created ever-increasing import dependence and has not encouraged local industry to supply the resorts, thereby dampening the multiplier benefits of these foreign investments.

Therefore, Caribbean nations might want to consider the model of welcoming multinationals only after imposing conditions that the firm develop and use only local suppliers for all of its intermediate inputs and abide by international labor standards. Such conditions can be set particularly if local and national governments are strong, but herein lies the weak link in the Caribbean's future.

Overall, according to Payne (1995), the political and social costs of international crime, neoliberal policies, population pressures, and an increasing lack of confidence that the political system can solve such problems is threatening the regional tradition and institutions of liberal democracy. Political parties cannot function effectively once in office; they are unable to address the problems of declining services and living standards and increasing poverty, unemployment, and crime. Moreover, because of pressing budget constraints and uncertain revenue streams, political leaders are no longer at liberty to dispense patronage as in the past.

The severity of international crime also bodes ill for the regions' future (Payne 1995): drug trafficking and money laundering syndicates have infiltrated and are corrupting governments, law enforcement agencies, and judiciaries. One concern is that entire island nations will fall under the influence of international criminal networks. For example, violent youth gangs, traditionally political in Jamaica, are becoming ever more connected to crime and drug addiction and introducing an element of anarchy into the social fabric of countries in the region. This shift in turn justifies totalitarian police methods and undermines the future.

Clearly, strong governance is key to a better development path in the Caribbean because its citizens now recognize the problems, threats, and uncertainties and view closer relations with the former colonial



power or the U.S. as a safeguard against political instability and economic decline. A small group of advocates for independence may remain active, but the quest for independence is now decidedly unfashionable in the Caribbean's former colonies. Given that the U.S. and Europe are concerned with the most populous island nations in the Caribbean, which Payne (1995:3) identifies as Haiti, Cuba, and the Dominican Republic, there is great cause for concern around the Caribbean basin. Moreover, there is no guarantee that betrothal to the metropolitan powers will provide the sought-after security. Based on the impediments to strong governance and the inescapable nature of globalization—both legitimate and criminal—the Caribbean is likely to sustain increasing difficulties into the twenty-first century.

### Selected Internet Sites

#### General:

ACS: Association of Caribbean States. [www.acs-aec.org](http://www.acs-aec.org)

CARICOM : Caribbean Community.  
[www.caricom.org/](http://www.caricom.org/)

CIA World Factbook.  
[www.cia.gov/cia/publications/factbook](http://www.cia.gov/cia/publications/factbook)

ECCB: Eastern Caribbean Central Bank.  
[www.eccb-centralbank.org](http://www.eccb-centralbank.org)

Miami Herald [www.miamiherald.com](http://www.miamiherald.com)

OECS: Organization of Eastern Caribbean States  
[www.oecs.org](http://www.oecs.org)

#### Aruba:

Aruban Politics.  
[www.visitaruba.com/facts/community/politics.html](http://www.visitaruba.com/facts/community/politics.html)

#### Barbados:

Barbados Workers Union.  
[www.bwuuccu.com/history.htm](http://www.bwuuccu.com/history.htm)  
Barbados Labour Party. [www.blp.org.bb](http://www.blp.org.bb)  
Barbados Elections:  
[www.caribbeanedu.com/elections/bb02.asp](http://www.caribbeanedu.com/elections/bb02.asp)

#### Cuba:

[www.granma.cu/ingles/index.html](http://www.granma.cu/ingles/index.html)

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### **Selected Video Referemces**

- Aristide: The Endless Revolution*, (2005) A Nicolas Rossier Film
- Life and Debt*, (2001) A Film by Stephanie Black. New Yorker Video

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## Catholic Social Teaching

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### **Introduction**

Catholic Social Teaching is a body of Church teaching found in a series of papal and episcopal documents of the Roman Catholic Church on matters of social ethics. The modern era of this teaching begins in 1891 and represents the Church's official response to pressing issues and situations within the larger global society and culture. Instead of offering specific policy initiatives, these teachings offer a vision of the human person and the common good in contemporary society through focusing on a set of themes (or principles). The major themes are: human dignity; solidarity; social justice; the common good; the rights of workers; subsidiarity; human rights; peace/disarmament; integral development; universal destination of goods; preferential option for the poor; and authentic freedom.

### **Emergence of Catholic Social Teaching**

The Catholic Social Thought tradition encompasses almost 2000 years of reflecting on social issues from the perspective of the Gospels. Modern Catholic Social Teaching is a reaction to the specific social problems that arose with the rise of capitalism in the later part of the 19<sup>th</sup> Century. In 1891, Pope Leo XIII released *Rerum Novarum* (*On the Condition of Labor*) to respond to the increasing exploitation of men, women and children in factories, the widening gap between rich and poor, and the rising political call for a socialist solution. For the first time, the Church placed the authority of Rome behind workers while simultaneously condemning socialism and communism. Despite its address to fellow bishops, *Rerum Novarum* aims at universal statements about the social condition of laborers compelling

even to those who do not share Leo's religious presuppositions. Out of concern for both the economic and cultural plight of the working classes, Leo attempts to carve out a theoretical agenda that is neither liberal nor socialist for a just society for the workers through focusing on *rights of workers* and *private property*. According to *Rerum Novarum*, everyone has the right to self-determination and to a just wage. *Rerum Novarum* explains, "If one man hires out to another his strength or skill, he does so for the purpose of receiving in return what is necessary for the satisfaction of his needs; he therefore expressly intends to acquire a right full and real, not only to the remuneration, but also to the disposal of such remuneration, just as he pleases" (RN 5).

Catholic Social Thought argues against communism and for private property: "The right to possess private property is derived from nature, not from man; and the State has the right to control its use in the interests of the public good alone, but by no means to absorb it altogether" (RN 47). *Rerum Novarum*, then, offers four arguments in favor of private property: the law of nature, private property distinguishes man from animals, the need to prepare for future generations, and the family as the primary unit of society in which the father has a duty to provide for the entire family (Shannon 2004:137). Through private property, the encyclical condemns any communist or socialist structure. This is not an endorsement of liberalism or capitalism. However, the critique of liberalism is considerably weaker than of communism and the encyclical is criticized for its acceptance of liberalism's understanding of private property. *Rerum Novarum* is clear, "Capital cannot do without labor nor labor without capital" (RN 19).

Forty years after *Rerum Novarum*, the immense unemployment and widespread poverty of the Great Depression in both

Europe and the United States provided the context for the second major papal encyclical on social justice. Released in 1931 by Pius XI, *Quadragesimo Anno (After Forty Years)* focuses on the relationship of the state and the common good. It focuses on the duty of the state through the themes of *subsidiarity* and *social justice*. The *principle of subsidiarity* insists, “Just as it is gravely wrong to take from individuals what they can accomplish by their own initiative and industry and give it to the community, so also it is an injustice and at the same time a grave evil and disturbance of right order to assign to a greater and higher association what lesser and subordinate organizations can do. For every social activity ought of its very nature to furnish help to the members of the body social, and never destroy and absorb them” (QA 79).

However, if the individual or community is not capable or refuses to solve a societal problem, then it is the responsibility of larger organizations or the state to intervene (QA 79, 80). The existence of intermediary groups between the individual and the state is integral to the function of subsidiarity. Subsidiarity requires that government be both as small as possible and as large as necessary. It does not specify how this operates in particular contexts. The second major theme introduced in *Quadragesimo Anno* is *social justice*. Social justice is a way to evaluate the justice of political and social structures: “The public institutions themselves, of peoples, moreover, ought to make all human society conform to the needs of the common good; that is, to the norm of social justice. If this is done, that most important division of social life, namely, economic activity, cannot fail likewise to return to right and sound order.” (QA 110).

“Social justice refers to the central and necessary set of conditions wherein each member is contributing, and thus enjoying all that is needed for the common good. But this

justice must be leavened and enlivened by the virtue of social charity or love (QA 88, 137)” (Hinze 2004:167). *Quadragesimo Anno* argues for an organic understanding of society based on the medieval guilds - corporatism. Some interpreted this as a third way. The tradition itself, however, explicitly rejects claims that it offers an alternative to socialism or capitalism. When it was released, “in the United States some Catholics used the encyclical to support the New Deal of President Franklin Roosevelt. ... President Roosevelt himself declared in Detroit on October 2, 1932 that *Quadragesimo Anno*, which he had just quoted, was ‘as radical as I am’” (Mich 1998:87).

### **Time of Change: Responding to Global Crises**

World War II sent the world into an uproar from which emerged two world powers, the United States and the Soviet Union, each vying for control of the world’s economic markets and governments. One of the characteristic features of the Cold War was the nuclear arms race between the US and the USSR. By the beginning of the 1960s, the tensions hit a breaking point. In 1961, Pope John XXIII released *Mater et Magistra (Christianity and Social Progress)* commenting on the nuclear arms race; furthermore, in 1963, months after the Cuban Missile Crisis he released *Pacem in Terris (Peace on Earth)* to emphasize human dignity and human rights. These encyclicals are distinctively modern in their approach and statements.

John XXIII addresses these encyclicals to *all people of good will*, in particular to the political and military leaders of the world. Peace and justice is the over-arching message in both encyclicals. *The common good, the interdependence of the global community, and human rights* are three main themes in John XXIII’s vision. *Mater et Magistra* defines the

*common good* as “all those social conditions which favor the full development of human personality.” (MM 65). *Pacem in Terris* expands this to include a *global common good*. Both documents emphasize repeatedly the *interdependence of the global community*. The nuclear arms race, and the danger it poses to the entire world, highlights this interdependence. *Human rights* include both civil-political and socio-economic rights. They are divided into levels of relationships (individuals, individuals and the state, between states), and at every level of society each right has a corresponding duty (PIT 8 – 144).

For example, “the right to live involves the duty to preserve one's life; the right to a decent standard of living, the duty to live in a becoming fashion; the right to be free to seek out the truth, the duty to devote oneself to an ever deeper and wider search for it.” (PIT 29). *Disarmament* is a key element to Catholic Social Thought's theme of human rights. “justice, right reason, and the recognition of man's dignity cry out insistently for a cessation to the arms race. . . .Nuclear weapons must be banned.” (PIT 112). Peace and justice only exist together. Peace requires justice and justice requires peace. Both the tone and themes of the encyclicals are optimistic about the possibility of achieving this peace and justice.

In the midst of this attention to the global context, the Roman Catholic Church turned its attention to its own self-identity as a global church with the Second Vatican Council (1962-1965). Begun by John XXIII and continued under Paul VI, Vatican II released many documents on the Church in contemporary society, including a Decree on Religious Liberty (*Dignitatis Humanae*). In the encyclical, “This Vatican Council declares that the human person has a *right to religious freedom*. This freedom means that all men are to be immune from coercion on

the part of individuals or of social groups and of any human power, in such wise that no one is to be forced to act in a manner contrary to his own beliefs, whether privately or publicly, whether alone or in association with others, within due limits.” (DH 2). Vatican II makes distinctions on the theological (sacred/secular), ethical (common good/public order) and political (society/state) to limit political authority and protect the religious freedom of individuals and religious communities.

In 1965 the Council released *Gaudium et Spes (The Church in the Modern World)* detailing the proper role of the Church and its members in contemporary society. Focusing on the human person and community, *Gaudium et Spes* emphasizes the need for responsibility and *participation* within political society. The encyclical states “All citizens, therefore, should be mindful of the right and also the duty to use their free vote to further the common good... Citizens, for their part, either individually or collectively, must be careful not to attribute excessive power to public authority, not to make exaggerated and untimely demands upon it in their own interests, lessening in this way the responsible role of persons, families and social groups.” (GS 75). Throughout the document, Vatican II offers an extended reflection on the necessary role of the Church and the faithful in a modern and global age.

After John XXIII, Pope Paul VI questioned the growing gap between developed and developing countries in light of the interdependence of the global community. Placing the issue of development at the center of his writings, Paul VI exposed *neocolonialism* and its connection to development. In 1967, he released *Populorum Progressio (On the Development of Peoples)* to emphasize the need for *integral development, and solidarity*: “The development We speak of here cannot be

restricted to economic growth alone. To be authentic, it must be well rounded; it must foster the development of each man and of the whole man.” (PP 14). This understanding of development offers a structural critique of neocolonialism and insists that private property must be understood within the context of the common good. In particular, “These words indicate that the right to private property is not absolute and unconditional. No one may appropriate surplus goods solely for his own private use when others lack the bare necessities of life.” (PP23).

Any attempt at promoting integral development must include “mutual *solidarity*—the aid that the richer nations must give to developing nations; 2) social justice—the rectification of trade relations between strong and weak nations; 3) universal charity—the effort to build a more humane world community, where all can give and receive, and where the progress of some is not bought at the expense of others,” (PP 44) to combat neocolonialism. Both individuals and nations must live up to their responsibilities to themselves and others, for, “The very life of needy nations, civil peace in the developing countries, and world peace itself are at stake.” (PP 55). Paul VI’s encyclical represents one of the first serious critiques of development theory of the time; however, it was criticized from both the right and left.

For example, “Michael Novak writing many years after its publication was anything but positive... Novak contended that the pope ‘lashed out’ at unrestrained liberal capitalism, condemning it as a ‘woeful system.’ Novak suggested that the problem with this encyclical is that the pope depended too much on the thought of third world development intellectuals.” (Deck 2004:308). From the left, it was criticized for not being critical enough of development; theologians like Gustavo Gutierrez expressed “Dissatisfaction with the word *development* . . . in what came to be

called the theory of dependency.” (Deck 2004:309). Furthermore, in 1971, Paul VI released *Octogesima Adveniens* (*A Call to Action*), a letter to the Pontifical Council for Peace and Justice. *Octogesima Adveniens* calls for greater attention to *urbanization and marginalization* in the developing world. In the wake of industrial development, “Man is experiencing a new loneliness; it is not in the face of a hostile nature which it has taken him centuries to subdue, but in an anonymous crowd which surrounds him and in which he feels himself a stranger. Urbanization, undoubtedly an irreversible stage in the development of human societies, confronts man with difficult problems.” (OA 10). The major concern with urbanization is the *marginalization* of workers and the lower classes.

The emphasis is on the development of the whole person and an attention to the common good. This includes active participation and taking responsibility through solidarity. “It is too easy to throw back on others responsibility for injustice, if at the same time one does not realize how each one shares in it personally, and how personal conversion is needed first. This basic humility will rid action of all inflexibility and sectarianism, it will also avoid discouragement in the face of a task which seems limitless in size.” (OA 48). In both documents, the emphasis is on the process of development and the need for it to be inclusive and protect the human rights of all. In response, “throughout the 1970s there were thousands of justice and peace organizations established within diocese and parishes. ... Catholic social justice lobbying groups were established to deal with local issues of poverty, racism, and violence, as well as with international and global issues of injustice.” (Gudorf 2004:330).

## **Responding to Globalization: The Social Philosophy of John Paul II**



All of the social problems of the twentieth century listed above continue today. The writings of John XXIII and Paul VI shifted the focus of Catholic Social Thought to issues of peace and justice in a global context. Continuing this development, Pope John Paul II uses his social encyclicals to simultaneously commemorate the work of his predecessors and offer his response to globalization. The first of these encyclicals is *Laborem Exercens* (*On Human Work*). Released on the ninetieth anniversary of *Rerum Novarum*, this encyclical returns to the beginning and the emphasis on the plight of the worker. It offers a reinterpretation of work, “to call attention to the dignity and rights of those who work, to condemn situations in which that dignity and those rights are violated, and to help guide . . . so as to ensure authentic progress by man and society” (LE 1).

*Laborem Exercens* is an extended theological reflection on the nature of work. The overarching theme of this document is that the human person is not created for work; work is created for the human person (LE 6). Any system of production must respect the dignity of the human person. To be human is to work. O’Brien and Shannon (1992) summarize the contribution of this encyclical stating, “Through work humans transform nature and personally fulfill themselves; work provides a basis for family life and the resources it needs; and through work persons affirm their membership in a nation and participate in attaining the common good. By working, human beings achieve a deeper realization of their personhood through a deeper participation in community and the common good” (351).

Furthermore, John Paul II argues for “*proposals for joint ownership of the means of work*, sharing by the workers in the management and/or profits of businesses, so-called shareholding by labour, etc” (LE 14).

Finally, as a theology of work, this encyclical emphasizes human work as a participation in creation: “the dignity of work consists of: it teaches that man ought to imitate God, his Creator, in working, because man alone has the unique characteristic of likeness to God. Man ought to imitate God both in working and also in resting, since God himself wished to present his own creative activity under the form of *work and rest*.” (LE 25). Different in tone and structure from the other encyclicals, *Laborem Exercens* commemorates the tradition by offering a reinterpretation of labor in a global context.

In 1987, commemorating the twentieth anniversary of *Popularum Progressio*, John Paul II released *Sollicitudo Rei Socialis* (*On Social Concern*). In the twenty years since *Popularum Progressio*, there has been “the full awareness among large numbers of men and women of their own dignity and that of every human being” (SRS 26). However, despite some progress, John Paul II uses this encyclical to show the work that still needs to be done. Renewing his predecessors call to action, John Paul II writes on the themes of *authentic development*, *global solidarity* and *the universal destination of goods*. True human development only occurs when all the important aspects of human life are part of this development: not only economic and material conditions but also spiritual, moral, religious, etc. (SRS 27-35)

Further, it is only right that people in all nations be given the opportunity for development in the true sense of the word (SRS 17). Development and interdependence are intimately linked. The authentic development of all peoples and nations is the right and responsibility of all. John Paul II clearly states, “Collaboration in the development of the whole person and of every human being is in fact a duty of *all towards all*” (SRS 32). *Sollicitudo Rei Socialis*, throughout the document,

emphasizes the need for development and solidarity to combat *structures of sin*: “a world which is divided into blocs, sustained by rigid ideologies, and in which instead of interdependence and solidarity different forms of imperialism hold sway, can only be a world subject to structures of sin.” (SRS 36). To combat this, John Paul II proposes the need for *global solidarity*. He states, “Solidarity helps us see the ‘other’—whether a person, people or nation—not just as some kind of instrument, with a work capacity and physical strength to be exploited at low cost and then discarded when no longer useful, but as our ‘neighbor,’ a ‘helper’, to be sharer, on par with ourselves” (SRS 39).

One of the basic principles of solidarity is that “the goods of creation are meant for all” (SRS 39). John Paul II explains that “The right to private property is valid and necessary, but ... Private property, in fact, is under a *social mortgage*, which means that it has an intrinsically social function, based upon and justified precisely by the principle of the universal destination of goods” (SRS 42). In this section on the universal destination of goods, John Paul II extends this beyond ownership of land and insists that “forms of technology and their transfer” must be understood within the framework of the universal destination of goods and genuine development (SRS 43). Laws and structures concerning intellectual property including technology and pharmaceuticals must be evaluated within the framework of the ‘social mortgage’ of private property and not as part of private property as an absolute right.

Refocusing the Church’s social teaching on the plight of the poor, the encyclical was warmly received by much of the developing world, while incurring criticisms in the Western “first-world” nations. Curran, Himes and Shannon (2004) offer examples of such criticism, “A U.S. representative to the United Nations also wondered whether it was fair to

put all the blame for poverty at the feet of the rich nations. In response, however, one Catholic journalist observed that a closer reading of the encyclical did not remove all blame for their plight from the poor nations themselves.” (431).

In 1991, John Paul II released *Centesimus Annus* marking both the hundredth anniversary of *Rerum Novarum* and the fall of communism in Central and Eastern Europe. The end of the Cold War meant a new political situation for the Church’s social teaching since the Church had spoken so strongly against both communism and socialism. *Centesimus Annus* reflects on all the themes of the earlier tradition. In particular, building upon the themes of authentic development, solidarity and subsidiarity, John Paul II defines and emphasizes the themes of *authentic freedom* and *human dignity*. Just as development cannot be understood purely in terms of material and economic development, economic freedom is only one aspect of freedom (CA 39).

The error of understanding freedom this way “detaches it from obedience to the truth, and consequently from obedience to the truth, and consequently from the duty to respect the rights of others. The essence of freedom then becomes self-love carried to the point of contempt for God and neighbor, a self-love, which leads to an unbridled affirmation of self-interest and which refuses to be limited by a demand of justice” (CA 17). True freedom and human development involves the freedom to pursue the truth (CA 46) against any understanding of freedom as relativism. Human persons are created for freedom, but “it cannot be forgotten that the manner in which the individual exercises his freedom is conditioned in innumerable ways” (CA 25).

The relationship of the individual to the community and the common good is here, and throughout the tradition. In order to have



authentic freedom, one must recognize and protect human dignity (CA 46). Human dignity is a focus of this encyclical and the tradition as a whole. The intrinsic value or dignity of the human person is at the heart of the traditions critique of communism (and John Paul II's condemnation of mechanism). The fall of communism does not represent an endorsement of capitalism on the part of Catholic Social Thought. The tradition did not endorse political liberalism or capitalism in its condemnation of communism, socialism and mechanism. *Centesimus Annus* offers a critique in light of the spread of capitalism. John Paul II is clear that "the inhuman inadequacies of capitalism are far from disappearing. In fact, for the poor, to the lack of material goods has been added a lack of knowledge and training which prevents them from escaping their state of humiliating subjection" (CA 33).

*Centesimus Annus* is the last of John Paul II's additions to Catholic Social Thought, however, the tradition continues with each papacy. Through his first encyclical, *Deus Caritas Est*, Pope Benedict XVI has begun to contribute to Church's social tradition. Like many of the earlier social encyclicals, *Deus Caritas Est* is directly addressed to the Catholic community. Beginning with a quote from 1 John, "God is love, and he who abides in love abides in God, and God abides in him" (1 Jn 4:16), Benedict XVI's purpose in this encyclical is to reflect on the reality revealed in Sacred scripture and its implications for living a Christian life. The encyclical proceeds in two parts, part one "the unity of love in creation and in salvation history" seeks to understand the nature of God, humanity and love. From there, part two, "*Caritas*: the practice of love by the Church as community of love," examines the human response to God's love through the service of charity.

## Further Application to Policy

Catholic Social Thought is not an alternative economic theory or social system (third way). Catholic Social Thought does not claim to provide all the answers to contemporary economic problems. Instead, it provides principles by which to guide our search for answers and criteria with which to judge economic and social outcomes. Its influence on public policy has been mostly indirect and typically has taken two forms. First, Catholic Social Thought has provided compelling moral arguments in favor of social and economic reform providing critical support in the political arena. Before *Rerum Novarum*, it was easy to marginalize and dismiss the union movement as "godless communism," after *Rerum Novarum* this was much harder to do. This was critical to the acceptance and legalization of unions in many countries.

Second, Catholic Social Thought has been the motivation for many individuals and groups who have pursued social justice, and thus has had a significant impact on public policy. Social reformers influenced by Catholic Social Thought have played key roles in writing the declaration of human rights, the development of the welfare state, the growth of labor unions, and more recently the efforts to cancel the Third World Debt (Jubilee 2000), rethink development in more human terms (changes in the World Bank in the past decade) and the living wage movement. To give just two examples. Firstly, it was after the United Nations held a conference on Paul VI's encyclical *Populorum Progressio*, which called for a rethinking of development policy in light of the centrality of the human person, and not merely promoting economic growth, that the United Nations started their efforts on the Human Development Reports. And secondly, the process by which the European Union was formed was started and directed by many individuals influenced by Catholic social

thought, and with the theme of “subsidiarity” being of critical significance.

\* All encyclical citations in this article are from [www.vatican.va](http://www.vatican.va)

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## Central-South Asian Political Parties and Policies

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### **Introduction**

Political parties constitute the institutional basis of a political democracy in the contemporary epoch. A study of political parties entails an understanding of their ideological orientation, political programs, policy frameworks, organizational structures, membership, electoral performance and history. Political parties provide the organizational basis for modern political systems, whether they are single-party or competitive multi-party political democracy. In a single-party led political system, the institution of the State has been seen to become fused with the only political party that leads the government and state institutions. Institutionalized norms of political democracy have a very weak institutional basis in such systems.

A multi-party political system provides for an institutional basis, although considerably imperfect, via the mechanism of periodic elections and changes in government. Both variants of political systems need political parties as distinct from the monarchical political systems of the past that survived for several centuries. In that sense the political party system is a very recent political phenomenon and is still undergoing evolution. Different variants of party systems were propagated by the proponents of modernist ideologies of liberalism and socialism. Multi-party political system primarily found favor with the exponents of liberal variants of ideologies, whereas single-party political system with those espousing socialist and communist variants of ideologies.

Modern day politics has been characterized by a contest between these two

competing ideologies and their different politico-ideological versions and adaptations. Recent times have witnessed an opinion that talks of primacy of economics over political, much in the same vein as some scholars have argued about the end of history. A logical corollary of such an argument considers democratic politics to be somewhat of an unnecessary institution that is anachronistic to the fast-paced economic development of the contemporary world. Such an argument ignores the centuries and millenniums of the evolution of the mankind, both intellectually and materially, and the historical legacy of diversities obtaining from the uneven growth in socio-cultural and politico-economic terms of reference. Politics, particularly democratic politics, is a way that has evolved to moderate the excesses, socio-economic, cultural discriminations and differentiations and deep cleavages of modern day society, economics and politics.

Political parties are relatively recent innovation in the history of evolution of the political systems. These were vital instruments of transition from a limited form of governance in pre-industrial and pre-modern era to an increasingly participative one with the devolution of economic, social and cultural power from an extremely restricted ruling circuit to wider sections of different societies. Formation and evolution of political parties addressed need for institutions that articulated the values, socio-economic interests and aspirations, along with historically determined needs of various sections of the society, in a broad sense. To work towards these goals, political parties as institutions sought to gain control over the State, the institution that societies crafted over time to govern themselves. In a political democracy the scope of those competing to rule and control the State increased as the society and the economy grew increasingly complex and more and more sections of the

society clamored for political participation and influence the ways and means by which they, and the society in general, were governed. Thus political parties became the via media or the channels for articulation through which various sections of the society sought to organize themselves, expand their political support, influence the politics of the day and achieve political power and the right to govern and lead the State through competitive political and electoral system in a multi-party democracy.

Political parties provided common platform to not only to those seeking political, economic and social reforms but also effected a gradual transfer of power and authority from restricted feudal circles onto much wider socio-political constituents. Such a clamor for political democratization was also a function of greater vertical and horizontal intellectual and cultural growth and expansion of consciousness along with vivid plurality of expressions of global human diversities in terms of their civilizational, cultural and social contents. Political parties emerged only in Nineteenth century in any significant measure on a global scale as tentative expressions of these diversities. Its intellectual and political leadership came, to a considerable extent, although not necessarily, from the middle and upper classes of these societies.

In many ways formation of political parties were the political rumblings and expression of an emerging civil society, a product of modernity of industrial societies that sought and eventually won, after significantly hard and bloody battles, the right to participate in the governance of their respective societies. Thus they broadened the scope of governance to include new and dynamic social and economic forces and gradually nibbled away power from the traditional family-based monarchies and feudaldom. It is a different matter that, over a

period of time, the emancipatory role played by the political parties as well as their structures too degenerated into electoral machines. Many of them became transformed to rigid and ossified ruling structures.

It took about a century of political churning and conflicts for political parties to establish themselves as the cornerstone of multi-party political democracies. However, both the political democracy and the political systems based on them, along with the contemporary form of governance, as well as the political parties that constituted the key conceptual, theoretical and operational basis of the former, have not acquired significant maturation as viable and terminal form of governance. They have by far only been the best available option of political governance and political system. The political parties that constitute the basis of political democracy themselves, for instance, need to democratize themselves.

In most cases, these as well as their policies and activities are influenced by rather unrepresentative sections of the political elite without any meaningful wider participation of their constituents. In effect either the mechanisms for such participation is non-existent or merely serve cosmetic purposes. Voting figures in most multi-party democracies makes obvious the limited reach of the political parties whereby a very large section of the electorate stays out of the process. In most cases, those who win the mandate to govern are actually recipients of minority votes of the overall vote's cast and still smaller percentage of overall electorate.

One of the major crises of legitimacy faced by multi-party political system has been that despite decades of existence they have been unable to ensure significant participation of electorates in the electoral processes, leave apart the political processes in their respective societies. A significantly large section of people, even the educated sections, stay

outside the process that determines the selection of the leaders that govern them and make laws and policies that are going to effect them. This is one of the fundamental weaknesses of a political system based on multi-party system that despite such a long existence it has failed to win the overall confidence of its constituents. Part of the reason, at least, lies in undemocratic structures of most political parties and the fact that they are controlled by limited sections of political elites, several times family based, thus unable to undergo periodic renewal and expansion, and depend on a largely 'conservative' core that acts as repository of the traditional values of these parties.

Moreover, in the contemporary era, most political parties have converted into vote gaining electoral machines and have given up their political role, an essential activity that had in the first place made them a recognized political force. With increasing role of media, a vital component of a modern political democracy, political imperatives of a society are being manufactured at a distance from the social constituents, with the latter being constantly told as to what it is and what it's political imperatives ought to be. This has alienated large sections of contemporary societies who may not have any influence on the opinion-makers and policy-makers as well as political leaderships.

A considerable middle-classization of politics and political parties has taken place. Such a process may have its positive dimensions but one of the key downside is alienation of a wide section of societies thereby restricting political democracy as a process of political expression, articulation and education. Political parties, albeit, have been evolving over a period of time and a political system based on political parties and competitive political systems offer an infinitely better alternative to authoritarian and undemocratic political systems, however

enlightened, benign or benevolent latter might be. The foremost reason for this is that the former variant of political system, with all its imperfections, offers an scope for the political expression of the diversity in any given society, making it difficult, if not impossible for any sectional or sectarian interest or interests to dominate the others at the expense of general good of all, particularly the majority constituents of any given society.

Furthermore, it offers better protection to the society in general against the possible excesses of the State system and its constituents like the bureaucracy and so on. In the absence of a competitive political democracy, as historical experience in different types of political systems at different points of time have amply demonstrated, the bureaucracy as the active arm of the system can come to dominate the imperatives of a society, fix its goals mostly substituting its interests as the interests of the former either deliberately or because of erroneous perception in the absence of a functioning mechanism to articulate the social, cultural and economic interests of any given society.

A political system based on multi-party democracy not only provides for the open expression of numerous given diversities that has been inherited historically in any society, it also provides opportunity for periodic ratification or otherwise by the popular opinion on the existing system of governance and its leaders or allow people to express their pleasure or displeasure through a referendum via a political vote from time to time. Although these are still considerably imperfect and conditioned, and often manipulated by several extraneous factors, even retrograde formations and ideologies, yet they do provide a social, cultural and economic and political expression and indices of the *existing* state of any given society.

Thus political democracy in many ways mirrors the society helping its constituents to

understand itself better and formulate the mode and practice of governance accordingly. This is the single biggest virtue of a political system based on competitive political democracy. Such a system also provides an opportunity to cure the pathological political elements of any given socio-cultural-political diversity that may otherwise remain subterranean in a closed modernizing political system through a process of political participation and rectification. A multi-party political system in itself is essentially a form of expression of varying political perspectives rooted in different sectional interests that are presented as universalized and ideological. This is then an interplay of multiple world views competing to win over hearts and minds, thereby providing different alternatives to choose from, rather than a single 'ultimate truth' of any variant, to adhere to for all times to come, even when it may have outlived its real or imagined political significance.

Modern day political parties project their perspectives as universal and terminal prescriptions of governance and good rule, and seek political mandate on these. Nonetheless political mobilization is also carried out in not any less significant manner on the basis of existing and given socio-cultural formations as well. This contributes in the expression of the given diversities. Thus modernist politicized and ideologized perspectives coexist with the given socio-cultural inheritances. Hence a sort of political and ideological dialectics mark the dynamics of contemporary politics and multi-party political systems. This contradiction is at the core of political transformations and maturation of political systems, political democracies and the ways and means by which a society not only seeks to govern itself but also how it relates to other contemporary societies.

Multi-party systems emerged in Central Asia in the post-Soviet era. Innumerable socio-political organizations and proto-parties mushroomed prior to the disintegration of the Soviet Union marked by a single party political system led by the Communist Party of Soviet Union. These evolved into a pluralistic political system with myriad political parties and political groupings. The party system is therefore still nebulous, unstable, in a state of flux and undergoing transformation. These countries have strong executives that tend to weaken the party-system. Nonetheless these parties represent the socio-political and cultural diversities in post-Soviet Central Asia.

In South Asia political pluralism has had more than five decades to develop after liberation from colonial rule. India has a well-established party-system and multi-party democracy. In Pakistan and Bangladesh, the political democracy and multi-party system has been interspersed with military rule. Former has a quasi party-system whereby a weak parliamentary multi-party system coexist with military rule. Latter currently has a parliamentary political party system. In Sri Lanka, party-system exists with a strong executive. In Nepal, nascent, a little more than a decade old party-system and political democracy was undermined by a resurgent monarchy. However, an anti-monarchy all-party political movement, with the political parties playing a vital role along with unprecedented popular participation, succeeded in restoring political democracy. In Myanmar, the military rule nipped in bud the experiment with democracy. In Maldives no political parties exist.

One of the most significant changes in political dynamics during the last two decades, particularly in South Asia, is the transition from one-party dominance to *coalition politics*. This transformation is particularly significant since it is indicative of

maturation and deepening of multiparty system in the region. Dominant single parties have given way to multiplicity of political parties reflecting the real diversities of social, cultural, economic and political forces in the region and their quest to articulate their interests through democratic channels. This has also greatly reduced the chances of political domination by a limited set of political leaderships that could resort to authoritarian or quasi-authoritarian measures. In current context, in the absence of any single political party overwhelmingly dominating the political system in circumstances where there is a lack of any viable or weak alternatives, as could happen in the past, groups of political parties with similar or considerably closer interests tend to negotiate coalitions distributing the power and ensuring a formal or informal system of checks and balances. This arrangement reduces the chances of undue or undemocratic domination of any of its constituents. It also provides better bargaining power to different constituents giving them a possibility of more effectively pursuing their political goals which could earlier have been ignored, apart from giving several groups and interests a possibility of being able to articulate their views and perspectives.

Thus an enhanced form of political plurality and diversity can be expressed via coalitions whether they are ruling or in opposition since these coalitions are often formed through a process of protracted political negotiations. ‘Closed’ and restricted coalitions of the past that were controlled and led by organizational structures of large political parties in single-party, single-party dominant and multi-party systems have been replaced by ‘open’ coalitions based on political negotiations. Finally, such coalitions bring about the involvement of a larger number of political actors than in the traditional one-party dominant systems,

democratizing the politics further and curtailing control of limited political leaderships via organizational structures and practices. This is the single-most significant transformation democratic political systems have undergone in this region in past two decades. The overall governance and policy framework of various political parties, wherever they exist, have been responsive to the changes in the era of globalization and the transformations it has ushered in.

### **Bangladesh**

Bangladesh has two leading political parties. The Bangladesh Awami League led the liberation movement of Bangladesh against Pakistan. Its key ideological plank is Bengali nationalism. It claims to be a “progressive, non-communal, democratic and nationalist” party with people's orientation and “progressive and pragmatic political, social and economic agenda”. (“50 Years of Struggle” website). This party emerged out of the national movement and occupies centrist and slightly left of the center political and ideological position in the politics of Bangladesh.

The Bangladesh Nationalist Party (BNP) supports free market economic system with the government playing the role of facilitator rather than regulator; of good governance and local level participatory planning. It claims to uphold Bangladeshi nationalism, people's participatory democracy and social justice. (Bangladesh Nationalist Party website). BNP emerged from the right-wing of Bangladesh army that usurped political power and imposed military rule overturning the gains of Bangladesh liberation movement and its establishment as a democratic nation. It essentially emerged as a right-wing and right of the center party supported by the right-wing elements of military establishment that was pro-Pakistan and never really accepted the liberation movement, and is supported by



the religious fundamentalist of a relatively moderate hue. However, in last years the party has tried to project itself as a conservative political party espousing economic reforms and trying to distance itself from religious fundamentalists and right-wing sections of the society projecting a moderate image.

## **India**

In India, regional political movement in Tamil Nadu in the South India raised the banner of Tamil nationalism. Dravida Kazhagam (DK) or Dravidian Federation movement committed to establishing an independent Dravid state grew into a regional party, Dravida Munnetra Kazhagam. It subsequently gave up the demand of an independent state and led a successful movement against Hindi being made official national language. In 1967 elections it defeated the Congress party and came to power in Tamil Nadu. The DMK and the AIDMK, all of which have their origins in DK, emerged as prominent regional political parties. Presently, however, the party ruling the state, the DMK is a prominent part of Congress led coalition United Progressive Alliance (UPA) that rules the Center, whereas the AIDMK, although non-aligned, had been part of National Democratic Alliance (NDA) led by the right-wing Bharatiya Janata Party, that is now in Opposition at the Center but was then the ruling coalition.

Thus the two major Dravida parties are very much responsible votaries of Indian federalism articulating both the regional as well as national concerns. Over a period of time regional political parties, although promoting regional political identities and local concerns have become increasingly strident in expressing their opinions on the issues of national concerns. This has been a major change in the national politics in recent times. Most of these parties are directly or

indirectly aligned to national level coalitions, either ruling or in opposition.

During 1980s the political hegemony of the Congress in Andhra Pradesh was successfully challenged by a regional party, the Telugu Desam that based its politics on local issues. The party was established by prominent star of films in the local language, Telugu, N T Ramarao. Although out of power in the province, until recent past it was an important constituent of NDA. A prominent regional political force in Punjab is Akali Dal that claims to represent the religion of Sikhism and bases its politics on Sikh identity. It came into existence in 1920s to control Gurudwaras or the places of religious worship. The party went on to play an active role in creation of Punjab as a Sikh majority state in 1960s. This party is a part of national coalition, NDA. The National Conference is a leading regional party of Jammu and Kashmir and was until recently aligned with NDA. Another regional party, the Peoples Democratic Party or PDP is part of the ruling coalition UPA both at the center as well as the state. These regional parties vouch for Kashmiriyat based on regional identity and are very much part of the mainstream national politics. Both parties, although supportive of local issues and regional identity, like other prominent regional parties, accept the Union of India, its Constitution and its unity and integrity.

The Assam Ganatantrik Parishad or AGP, evolved from a student organization and movement, the All Assam Students Union in 1980s. Its politics rests on a call to Assamese nationalism in opposition to immigration of Muslim Bengalees from neighboring Bangladesh. This movement in its initial phase took a chauvinistic turn and even opposed the presence of Indian Bengalees. Its political appeal is based on the fear of people of Assamese origin being eventually reduced to a minority in the province and becoming

culturally marginalized within its geographical boundaries. However, after leading a turbulent and very violent separatist movement in the past, it came back to the mainstream of the national politics, established its identity as regional party, got divided in recent past, aligned with major national political parties and eventually integrated itself with the mainstream national and regional democratic politics. These inspired the formation of rather smaller sub-regional party based on sub-regional identity that have made their presence felt currently as important, albeit smaller regional political entities participating in democratic politics of the province.

Some parties like the Samajwadi Party (SP), primarily strong in the northern province of Uttar Pradesh, and Rashtriya Janata Dal (RJD) based in Bihar, appeal to a rather indigenous version of socialism based ideologically on the interests of so-called backward classes and a strong defense of minorities and secularism. In last decade or so both the parties have sought to extend their appeal to other sections of the society, particularly the upper castes. They support the ruling coalition UPA at the center, former, the SP, indirectly, maintaining a rather uneasy relationship owing to its conflict of political interests in Uttar Pradesh with the leading constituent of UPA, the Congress party, particularly with the impending state-level elections. Latter, the RJD, in opposition in the state of Bihar, having lost the recent elections to the NDA is an unconditional ally of the Congress and the constituent of UPA. However, latter's alliance is of a strategic nature whereas the formers seems tenuous and based on single issue of secularism. Another political party that preaches indigenous variant of socialism is Janata Dal (United) and is the leading constituent of the coalition that rules state of Bihar. A similar

regional party Biju Janata Dal rules Orissa in alliance with Bharatiya Janata Party.

Such indiginity in some variants of homegrown concepts of socialism have found lots in common with the right-wing Hindu nationalist forces and have entered into strategic political alliance with them. Another example of such a regional force is Trinamool Congress in West Bengal. Parties like Bahujan Samaj Party, essentially regional in nature, with its primary presence in Uttar Pradesh, articulate the interests of Dalits or the Scheduled Castes. The party has based its appeal on the consolidation, articulation and mobilization of Dalit identity that represents the most downtrodden section of the Indian society. This party was earlier a part of the NDA when it ruled at the center. Presently it is not aligned as such to any coalition although it supports the ruling UPA. (Data-1995, SASNET).

The Nationalist Congress Party, the ruling coalition partner of the Congress in the Western state of Maharashtra is also a part of ruling coalition UPA. It has a significant provincial presence and seeks to primarily highlight regional issues. However, as its name suggests, it claims to adhere to a national perspective. Shiv Sena, an ethnicity-oriented regional party from this state and a part of opposition NDA at the Center has shown strong and often extreme proclivity of appealing to communal politics and right-wing Hindu nationalism. However, it also claims to appeal to regional issues occasionally verging to militant provincial chauvinism, primarily because of some kind of belief in ethnicity-oriented provincial politics, in its strident advocacy of what it perceives as issues relevant to the region. A political regionalism based on federalism in a country with wide and vivid diversities is more in sync with a multi-party political democracy than ethnicity-oriented provincialism in a political democracy since

the latter often introduces a false sense of ethnic superiority resulting in ethnicity based cultural and political chauvinism. Parties like Jarkhand Mukti Morcha have been based on sub-regional and tribal identity that was politicized over a long period of time.

*Table 1. India: List of National Parties*

<b>National Parties</b>
Bahujan Samaj Party (BSP)
Bharatiya Janata Party (BJP)
Communist Party of India (CPI)
Communist Party of India (Marxist) (CPI(M))
Indian National Congress (INC)
Janata Dal (JD)
Samata Party (SAP)

The Congress party that led the nationalist movement in India and dominated its politics for first forty-five years after India became independent in 1947, continued to be a major political force as the second largest political party and the main opposition party in the previous parliament, its longest spell in opposition. In present parliament, it is the largest political party having won 145 out of 543 seats. Although a pale shadow of its formidable past, when it led a one-party dominant political system, it nonetheless command roughly a quarter seats and lead the ruling coalition the United Progressive Alliance (UPA) in the present parliament and is supported by the Left Front from outside.

The party espouses an admixture of liberal, social-democratic and socialist political ideologies and is more like a political platform reflecting different ideologies and political groupings. The Party itself is like a political coalition with different political ideologies and perspectives having been dominant from time to time depending on the flavor of that particular period. After Jawahar Lal Nehru, it is rather difficult to contend that the Party had a coherent political and ideological position. Its dominant political and ideological positions have fluctuated from mixed economy variant to socialistic to

neo-liberal reformistic orientations. Party had primarily been a pragmatic political formation rather than a stickler to any specific political ideological positions and policies. Decades of political dominance in a one-party dominant political system in its post-colonial phase, the political values that the party had imbibed in its anti-colonial, anti-imperialist era that informed its political ethos got substantially eroded, particularly after Nehru.

The Declaration of Emergency in 1975 was the lowest point in its history when political authoritarianism seemed to have thrown away all the gains made during anti-colonial, anti-imperialist struggle of Indian people. A strong reaction to such an act gave a significant fillip to the opposition movements and political parties and groupings that have hitherto been confined to the provinces. For the first time, combined opposition that included the entire spectrum of political opinion, directly or indirectly, came to power for a brief period in 1977, ousting Congress from the national level and decimated its unchallenged political hegemony in Independent India. A couple of decades later Party disintegrated and went into political wilderness for eight long years only to return to power in 2004 at the head of a coalition with considerably reduced numbers and shored up by the support from the left alliance primarily on the issue of secularism in circumstances whereby the right-wing Hindu nationalist party, the BJP led NDA coalition that displayed strident anti-minorityism and blatant majoritarianism, was in power for six of these eight years.

The Party won a little less than three-quarters of the parliamentary seats until 1967. People of India recognized its role in the independence movement along with those of numerous other groups and organizations. For several decades after Indian independence, it was the only political party with a nationwide presence forged during freedom struggle. The

party took into account the local specificities and incorporated local leaderships in its fold. It disbursed economic and political resources and patronage thereby ensuring its political hegemony for a long time even when its political role and values have been severely undermined.

From 1967 onwards, the party started losing its dominant position in Indian political system and by 1990s it was in the throes of severe crises, disintegrating and emaciated. Emergence of post-independence generations, new groups and political interests and the inability of the party to contain them within its fold; dissidence and defections; politically authoritarian actions like imposition of Emergency; series of splits in the party; disruption of the social coalition or its traditional social foundation that had been its main base delivering political power to the party one election after another; lack of inner party democracy; personalization and centralization of the party; its inability to adjust to the major social transformations that had taken place in the country; policies of unbridled liberalization and privatization of the economy and its desperate attempts to play the "Hindu Card" in 1989 denting its image as a secular and largely democratic party, were some of the reasons that contributed to its unchecked decline, not only in its electoral fortunes, but also in its political influence. (Data-1995, SASNET).

During its long existence it had come to adhere to the values of socialism, nationalism, democracy and constitutionalism. (Brass & Robinson 1987:10-11) These values eroded in its latter years. In its heydays it was the party of consensus in a One Party Dominant System with opposition at best functioning as parties of pressure. (Kothari 1964). Such a characterization has also been supported by other scholars. (Jones 1964). The party owed its success to its resilience and its ability to absorb new elite groups in post-independence

period. (Weiner in Joshi & Hebsur 1987:289). It attracted some "dedicated modernists" in the past because of "its stand for national integration, secularism and representative government" (Weiner 1967:474).

In 1980s and 1990s, most of these basic values had been considerably eroded, partly as the politics of convenience and power in an electoral democracy replaced the politics of values as a centrist political force, and partly because global and national circumstances had undergone significant changes with the demolition of bipolar world. The dominant contradiction between the so-called liberal and socialist world-views that dominated post-Second World War world was replaced by a multi-polar world and a resurgence of so called primordial loyalties and multiple world-views along-with the ascendance of neo-liberal economics and market as the credo challenging communitarian ideologies of socialism and presenting individualism as the only alternative left for a so-called 'new world'.

These resulted in a crisis of identity and orientation faced by most modernist political forces. In the new millennium most of these political parties are trying to find their feet and resurrect relevant modernist identities, picking up pieces after what may hopefully be the final resurgence and abatement of the subterranean primordial political forces that have rather little relevance. Latter were a response to the excesses of modernist political forces and the current phase is witnessing an attempt to revive a moderate face of modernism over the 'ruins' of a so-called 'old world order'.

The Bharatiya Janata Party (BJP) is a Hindu nationalist party of Right with religious-cultural nationalism as its ideological basis. It appeals to an identity based on a particular variant of Hindu religion. It is the political front organization of Rashtriya Swayamsevak Sangh (RSS) or National Volunteer

Federation, a self-proclaimed Hindu organization that likes everybody to believe that it is a purely cultural and not political in nature (not many, however buy this self-characterization of RSS and consider it be the political core of BJP and Hindutva politics), claiming to work for the cause of Hindu religion. It endeavors to build a Hindu India based on the philosophy of Hindutva or Hindu Nationalism. The RSS belief system has been defined as representing a kind of militant Hindu nationalism and is closely related to the evolution of Bharatiya Janata Party and its predecessor (Andersen & Damle 1987). The BJP is part of Sangh Parivar or the 'Family' headed by the RSS. Latter constitutes the backbone of its political affiliate, the BJP. BJP's predecessor the Bharatiya Jan Sangh was established in 1951 to mobilize people and come to power on the basis of their religious affiliation to the majority Hindu religion.

The party was closely identified with the upper caste, North Indian, Hindi-speaking, exclusive and elitised Brahmanical Hinduism, and failed to make much headway in electoral terms or political influence. In 1977, the Bharatiya Jan Sangh merged with Janata Party that defeated Congress in the elections after the proclamation of Emergency was withdrawn. It participated in the government formed, left the folds of the Janata Party and reappeared in its current avatar as BJP. In 1980s and 1990s, the party grew rapidly and came to power on a plank of anti-minorityism and the issue of Babri Masjid-Ram Janam Bhoomi Temple, using religious identity-based politics and a populist and bloody agitation that finally led to the polarization of a section of majority community.

Left parties too play a prominent role in Indian politics. The first democratically elected communist state government was formed in Kerala in 1957 and was dismissed by the central government in 1959. In 1964,

the party split into the Communist Party of India (CPI) and the Communist Party of India (Marxist) or CPI (M). In 1967, the CPI (M) underwent another split by a Maoist faction. A Maoist party, the Communist Party of India (Marxist-Leninist) was formed in 1969. A united left could have played a significant role in Indian politics. The CPI (M) increased its vote share from 4.2 % in 1967 to 6.7 % in 1991, although mostly confined to the states of West Bengal (where it has been voted into as head of a coalition government continuously since 1977), Kerala and Tripura, whereas that of the CPI declined from 5.2 % in 1967 to 2.5 % in 1991.

According to one of the leading scholars on Indian Left, the Left parties in India are too engrossed and involved in fighting the scourge of communalism or sectarianism, defending secularism and national unity so much so that "the class battles and struggles for the economic relief to the people as part of the moves to keep the class question as the focal point of the politics have been pushed into the background" (Alam in Hasan 2002:289). The left, along with other democratic and secular forces, became the rallying point for secular and democratic forces in the 1980s and 1990s when the Indian composite social and political fabric came under severe strain from resurgent political forces seeking to divide the country along communal and sectarian lines. Disintegration of centrist and centrist-leftist political forces created a political vacuum temporarily filled up by communal, right-wing and majoritarian political forces. Present trend shows an increasingly united left evolving a Left Front based on common issues, leaving aside ideological bickering of the past, and is playing a key role in defense of democracy, secularism and economic and political rights of Indian people.

The Left parties talk of fulfilling the aspirations of all sections of the working

people, promoting self-reliant economy and growth; implementation of radical land reforms and public investment in agriculture; employment; right to work; expansion of public sector; equal opportunities and reduction of inequalities. They seek separation of religion and politics; prohibiting the use of religious issues for electoral purposes; protection of the basic right of religious belief and practicing one's religion; a federation based on renewed Center-State relations in contrast to a nationhood based on Hindutva; fulfilling democratic aspirations of peoples of diverse cultures and language groups within a united and federal India; socio-economic justice and protection of the rights of minorities; strengthening of parliamentary democratic system and guaranteeing the secular-democratic basis of Indian Republic and its unity and integrity. (Left Parties Manifesto, 1998).

The left parties, however have never come to power nationally on their own, particularly because of lack of any significant presence in North India, but have supported national parties or coalitions in the Center. Currently they support the ruling UPA led by Congress from outside without participating in the government.

There are 654 political parties in India that include 7 national parties (Bahujan Samaj Party, Bharatiya Janata Party, Communist Party of India, Communist Party of India—Marxist, Indian National Congress, Janata Dal and Samata Party); 35 state-level parties and 612 registered parties but unrecognized parties in 2003.

## Myanmar

Myanmar (Burma) is ruled by the military. A *Pyithu Hluttaw* (People's Assembly) elected May 1990 with 489 members was not allowed to meet. Only military backed *Taunggyintha Silonenyinyutye* (National Unity Party) exists. Opposition National League for Democracy

won over 80 per cent of the seats in Burma's 1990 parliamentary elections but has not been allowed to form a government. It remains one of the rare political system in which the entire nation is in overwhelming grip of military rule. A brief attempt to introduce political democracy was aborted by the generals.

The Majlis (Assembly) in **Maldives** has 48 members. 40 members were elected for a term of five years and 8 members were appointed. The elections are on non-partisan basis and no political parties exist.

## Nepal

Nepal has a political democracy that was briefly interrupted by the King of Nepal on tenuous grounds that the political parties were not able to control Maoist insurgency in rural hinterland. He suspended the parliament and the political democracy in Nepal and a return to outright monarchy was imposed. His attempts to introduce a controlled democracy at the local levels, in effect doing away with parliamentary democracy and re-imposing absolutist Monarchy with the help of Royal Nepalese Army and loyal courtiers, as well as his failure to be able to do much about the Maoist rebels resulted in a mass uprising against Monarchy led by a Seven-Party Alliance. The Alliance not only led a revival of political democracy after bloody clashes in which several people were killed, but also succeeded in working out a peace plan with the Maoist paving the way for their integration in the mainstream democratic politics of Nepal (and brief leadership in government in the late 2000s). The Nepalese legislature has severely curtailed the powers of the King, putting in doubt even his role as a constitutional Monarch in any future comprehensive political settlement.

In Nepal, the Nepali Congress (NC) Manifesto identifies its ideological-political underpinnings as Nationalism, Democracy and Socialism in a multi-party parliamentary

democracy and a Constitutional Monarchy. Democratic socialism and decentralization form the cornerstone of its domestic policy. It seeks to promote private sector as well as welfare state. The party supports the neo-liberal economic policies with increased privatization of the economy; international investments; multi-national companies; foreign grants and loans; develop Nepal as a center for international finance and banking and favors regional economic cooperation in South Asia in response to the globalization process and the resultant "stiff competition in world market". (The Nepali Congress Manifesto: Highlights)

Communist Party of Nepal (UML), the other major political force, calls for social revolution in Nepal. UML seeks the consolidation of a self-reliant national industrial economy based on the development of the national capital to achieve the goal of socialism. Scientific socialism and communism are its ultimate goals and Marxism -Leninism the guiding principle. The Party accepts the supremacy of the Constitution; multi-party competition and Constitutional Monarchy; pluralistic open society; rule of law; formation of the government by the party in the majority; opposition of the party in minority; human rights; democratic fundamental rights and constitutional guarantee and safeguard of peace, characterizing the system as that of people's multi-party system. It accepts the theory of separation of powers and a constitutional welfare state. It supports a mixed economy with the state playing a leading role. Private sector is encouraged and despite believing that neo-colonial exploitation continues individually or via international financial institutions, foreign capital and technology is acceptable to the Party. (The Manifesto of the Communist Party of Nepal - UML)

## **Pakistan**

Some scholars believe that Pakistan was an experiment in "Islamic Democracy". The 1956 Constitution characterizes it as "a democratic state with its ethical aspect via Islam". (Golam W. Chaudhry, 1988, p. 233) For most of its existence Pakistan has been under military rule. Its brief encounters with political democracy have been turbulent, troublesome and temporary. Although not a theocratic state, Pakistan has been under religious and ideological influence of Islam. Party-based political system and representative democracy could not mature and stabilize in Pakistan primarily due to the interference of the Army time and again.

Recent elections in Pakistan, under the shadow of military rule, resulted in a hung assembly. The Pakistan Muslim League-Quaid-e-Azam (PML-QA), the President's party, won 77 out of 268 directly elected seats followed by the Pakistan People's Party Parliamentarians (PPPP) of Benazir Bhutto. The Muttahida Majlis-i-Amal (MMA), an alliance of six religious parties won 11% votes with 45 or 18 % of National Assembly seats bringing them to the center stage of the politics in Pakistan. It campaigned against the United States war on terrorism and their presence in Pakistan. They won 80 % parliamentary seats in North-West Frontier Province (NWFP)' control the government in this province and provincial coalition government in Baluchistan. (South Asia Monitor, [Two Elections: New Hopes and Old Frustrations, South Asia Program, Center for Strategic and International Studies, Washington], Number 52, November 01, 2002).

Zulfikar Ali Bhutto established Pakistan People's Party or PPP, in 1967. Its proclaimed ideology was that of establishing an "egalitarian democracy" and "the application of socialistic ideas to realize social and economic justice". It had following

principles: (a) "Islam is our faith"; (b) "Democracy is our politics"; (c) "Socialism is our economy"; and (d) "All power to people". The Party program underwent change in 1992 under the New Social Contract initiated by Benazir Bhutto that "envisaged a social market economy, privatization of the means of production, downsizing of the government, devolution of power and decentralization to the level of Local Government". (Manifesto of the Pakistan Peoples Party)

Jamaat-e-Islami wants an Islamic revolution in Pakistan with education, the Constitution, the laws and the Judiciary molded according to the Islamic ideology. They lay special emphasis on trade and economic relations with the Ummah or the Muslim Community. Jamaat seeks to encourage private entrepreneurship and a "careful" and "balanced" privatization of the public sector. (Qazi Hussain Ahmed, Jamaat-e-Islami—Our Programme: An Islamic Revolution, *The Jang*, Rawalpindi, August 27, 1997) Globalization is seen as a measure to control the financial resources of the Muslim world, impose on them western culture and civilization and colonize them. It wants to take Pakistan's economy out of "the snare of transnational financial institutions and global colonialism". (Khurshid Ahmed, (Naib AMEER, Jamaat-e-Islami, Pakistan), *Pakistan : Crises and the Way Out*, Tarjuman al-Quran, October 2000)

### **Sri Lanka**

In Sri Lanka the political system is deemed to be rather centralist in nature with more power concentrated at national level institutions and thus weak local level political and politico-administrative institutions. (Mick Moore, 1985, p. 228) The 1995 Peace Proposals of the Sri Lankan government have sought to increase the provincial powers decreasing the possibilities of central intervention, removed the provision of "shared" powers and defined

Sri Lanka as "an indissoluble union of regions" (*South Asia Monitor*, Jan 2003). The roots of present day politics in Sri Lanka lies in the pre-independence past when "Strategic ethnicity" was practiced by political groups and parties trying to maximize power and "reactive ethnicity" by those groups that were threatened. Thus ethnicity was "a crucial political resource for all parties concerned" and became an important basis for future Sri Lankan society and politics. Some studies demonstrated that secular politics gave way to religion-based politics over a period of time (Wickramasinghe 1995:xxi-xxii). In ethnic politics, race was "the main identity marker". "Ceylonese nationalism", which manifested at independence, was essentially "the expression of a Sinhalese Buddhist ethnicity". Disenfranchisement of Indian Tamil in 1948-49 and declaration of Sinhalese language as the only official language gave a fillip to minority Tamil ethnicity (Wickramasinghe 1995:255-258). Thus the basis of contemporary polarized ethnic politics was laid and strengthened. Nationalism and institutions based on them could not become the basis of Sri Lankan polity that could bring about a historic compromise and participation of various ethnicities. In case of Sri Lanka it is not merely an ethnic but a religious divide as well with Sinhala majority practicing Buddhist religion whereas minority Tamils being Hindus.

United National Party (UNP) talks of a stable government and "a proud Sri Lankan identity" in a country divided on the basis of race, religion, region and political ideologies. Its economic policy is based on "a people-oriented developmental plan". It talks of entering the world market, encouraging competitive enterprise and foreign collaborations. Its economic program is based on the concept of mixed economy involving private and public sector. UNP calls for a negotiated political settlement for the ethnic



strife in Sri Lanka involving a dialogue between the political parties, the clergy, the civil society and the LTTE as well. (UNP Election Manifesto, website UNP)

Sri Lanka Freedom Party (SLFP) was established in 1951 by S W R D Bandaranaike. He had organized the Sinhala Maha Sabha in 1937 in order to promote Sinhalese culture and community interests. Socialism was added to it after independence along with primacy of Sinhalese language and Buddhist religion. In contrast to the free market orientation of the UNP, the SLFP's policies have included economic self-sufficiency, nationalization of major enterprises, creation of a comprehensive welfare state, redistribution of wealth, and a nonaligned foreign policy. (Sri Lanka Freedom Party, LOC website). Presently it is a party of social-democratic orientation in contrast to the conservative nature of UNP.

*Table 2, Sri Lanka Presidential Election Results, 2005*

Candidate	Party	Votes	%
Mahinda Rajapakse	United People's Freedom Alliance	4,887,152	50.29
Ranil Wickremesinghe	United National Party	4,706,366	48.43
Siritunga Jayasuriya	United Socialist Party	35,425	0.36
Other Parties (10)			0.80
<b>Total</b>		<b>9,717,039</b>	

Source: Adapted from Electionworld.org, "Elections around world"

A fundamental problem with promoting a politics based on specific religion, ethnicity or culture, is that it is sculpted on the basis of an 'other' or an internal alien thus creating fundamental socio-political fissure or fault-lines, however egalitarian or modernizing the economic system might be. In primitive stages of political democracy, political forces tend to utilize readymade and inherited socio-

cultural diversities to mobilize support. Whatever justification for these in political democracies as means to reflect socio-cultural diversities, these often give expression to extreme, exclusivistic, chauvinistic and violent forms of political identities and praxis on either side of the political and socio-cultural divide that takes generations to heal and mitigate the damage done to the socio-political fiber.

All the South Asian countries are part of Indian sub-continent and thus share considerable civilizational and socio-cultural similarities that are reflected in the contemporary politics. Plurality and nature of South Asian politics and political parties and state of political democracy, albeit in different stages of evolution because of varying nature of political systems, nevertheless share a great deal of commonality. In all the countries of South Asia, political mobilization and political democracy based on modernist project involving liberalism, socialism, communism, social-democracy coexists with those based on religion, region, sub-regions, caste, tribal identity, ethnicity and so on. Political systems range from parliamentary, presidential, multi-party systems to military dictatorships and non-party systems. Thus contemporary South Asian politics is characterized by the coexistence and competition of modernist and civic politics and mobilization with those based on socio-cultural identities.

### **Political Parties & Policies in Central Asia**

Political parties in Central Asian countries lack broad social base; do not adequately represent various sections of the society or influence the popular opinion; are small and organizationally weak; revolve around personalities and are influenced by the state. They originated from socio-political movements and clubs that mushroomed during Perestroika. Several of these were

nationalist in character seeking to promote their indigenous ethnicity and local cultures and languages. In post 1991 phase these political formations - political parties, public organizations and movements were given legal basis to participate in elections of new nations that emerged as a result of the disintegration of the Soviet Union. Party system, therefore, is in its very early stages. Political parties will thus take a long process of permutations and combinations to evolve into viable political entities with well defined political perspectives as different from being centered around one or more political issues, develop organizational structures and ideological ethos to stabilize as a coherent part of a political system.

Several of the existing proto-parties will either disintegrate, or merge with other political entities or mutate into other forms before an established party system emerges. As the political democracy and the party system in these new nation-states mature it will give rise to a fewer number of parties based on more comprehensive world-views and socio-political and economic interests than there are currently. Advanced multi-party systems have reflected maturation into lesser number of political parties or political coalitions characterizing their political systems. This is because of smaller parties, proto-parties and groups either merging with larger entities or merging with each other to form a broader political platform to maximize electoral and political benefits; or because of ideological proximity between smaller groups or parties that renders existence of more than one political party quite unnecessary or irrelevant or simply the disintegration of smaller political parties over a period of time. However a trend towards unifications have simultaneously been accompanied with a tendency towards the formation of civil society groupings based on limited social and civic issues or even political issues,

particularly over last three-four decades. This does indicate the inadequacy of larger political parties and the system of political democracy to be able to address several issues concerning people.

However, the active constituents of both political parties and these groupings have been burgeoning. The formation of larger political entities, however display a tendency and inherent danger of becoming ossified and becoming politically authoritarian unless the members of the society and the political leaderships of these parties display a conscious attempt to keep this tendency in control. Thus a form of political dialectics characterizing the formation and reformation of political parties is evident. This is what makes the process of democratization of the political parties themselves of utmost importance in the contemporary phase of political party system and political democracy.

Following the collapse of USSR, Central Asian republic leaderships hastily mobilized dominant or majoritarian national identities commensurate with their territories. (Renel R. Hanks 2000:942) Perestroika and Glasnost had enabled overt political, ideological and organizational mobilization of ethnicity-based groups. Most of these displayed ultra-nationalist characteristics verging on chauvinism and were directed against Russianism considered synonymous with the communism of Soviet Union. Economic crises and resultant economic and political disruption contributed to immense unpopularity of the political class of erstwhile Soviet Union with nationalism based on ethnicity emerging as key political alternative. Regional political mobilizations have been another vital ingredient of Central Asian politics.

Ethnicity thus is an important ingredient of politics in *Kazakhstan*. Although Kazakhs are a minority with a population of 39.7%

followed by Russians with 33% (Schatz 2000:489), yet out of 320 top political appointees and members of parliament, 70.9% were Kazakh, 23.4% were Slavs and 5.6% from other backgrounds. The chair of Majlis and Senate, as well as the Presidency were open only to those with “fluency in Kazakh” thereby restricting them practically for Kazakhs (Schatz 2000:495). Nursultan Nazarbaev, the President, attempted to reconcile civic and ethnic nationalisms through “a peculiar synthesis of the national sovereignty of Kazakhs and the sovereignty of the people of Kazakhstan in general as an ethno-political community” (Kolsto 1998:56). Azat, Alash and Zheltoqsan were openly nationalist Kazakh political groups. (Kolsto 1998:65)

The Communist Party of Kazakhstan (CPK) believes in the principle of scientific socialism and human ideals; seeks to restore Soviets; establish a parliamentary republic; promote mixed economy with socialist type ownership in private and state-owned form; planned management of national property; restore of Soviet type social guarantees; ensure state control over foreign trade and provide free healthcare and education. Agrarian Party favored introduction of private property in agriculture and claims to be a conservative political force. Republican political party "OTAN" was created as the party of the President by merging parties like National unity of Kazakhstan, Democratic Party, Liberal Movement of Kazakhstan and “For Kazakhstan—2030” Movement. “People’s Congress of Kazakhstan” talks of creating a humane, democratic society; law governed state and supports gradual privatization of the state property and land. Republican People’s Party of Kazakhstan (RNPK) aims to create a democratic state with a socially oriented market economy. Party of Revival of Kazakhstan (PRK) claims to promote “moral and spiritual revival of

society, creation of civil society and state ruled by law with socially oriented economy”.

“Azamat” stands for local self-government; against unbridled selling off of national economy to multi-nationals; favoured open ownership of property; de-monopolization of economy and the banking system; supports national bourgeoisie and promoting welfare schemes. "Alash" seeks to revive Kazakh nation and claims to represent the interests of the Kazakh population. Republican Political Labor Party (RPLP) identifies intelligentsia; promotes democratic values and human rights; political pluralism and opposes ideological monopoly. Civil Party supports increase in production, improvement of living conditions and a strong and sovereign Kazakhstan.

Political Parties in Kazakhstan grew out of at-least 243 religious and public associations registered by the Kazakhstan Ministry of Justice. These, along-with 15 other groups and factions, had merged in 1992 to form Social Defense Coalition opposed to the leadership of Nursultan Nazarbaev. This platform included diverse parties and groups like radical nationalist "Alash", Russian minority dominated "Yedinstvo", Kazakh nationalist "Azat" movement, Kazakhstani People's Congress Party (NKK), "Zheltoksan" Party, Kazakhstani Independent Trade Union Center, Kazakhstani Helsinki Group, the Workers Movement, the “Adilet” society and the Kazakhstani “Memorial”. They were opposed to the presidential system of government.

In **Kirgizstan**, eight political parties registered themselves with the Ministry of Justice by the end of 1993. These included Agrarian Party, Republican People's Party, Party of Communists of Kirgizstan, “DDK” Party, “Ata Meken” Party, “Erkin Kirgizstan” Party, “Asaba” Party, and Social Democratic Party. (Srivastava 1999:250-252) In Kirgizstan, “public space” has been created

by the political elites but it has not been "fully institutionalized" and is vulnerable to subversion or being restricted (Anderson 2000:80). This has created conditions for "a more benign political path" (p.90). However, the February 1995 elections have deepened social divisions along ethnic lines with minorities like Russians and Uzbeks getting significantly less number of seats in a Parliament overwhelmingly weighed in favor of ethnic Kirgiz (Huskey 1995:828-29).

Immediate post-Soviet experience of **Tazikistan** was marked by "personal intrigues, regional conflicts and ethnic bloodshed" (Akbarzadeh 1996:1105). The elections in 1995 to Majlisi Oli, the Parliament, were held in "dubious circumstances". Regionalism or "*mahalagaroi*" is seen as a "built-in defect" in Tajik politics. Islamic symbolism has been used increasingly and the emphasis on the Tajik language as an official language by the Tajik opposition espousing national assertiveness has made minorities suspicious of them. A combination of "*mahalagaroi*", nationalism and ethnic resentments constitute the basis of Tajik politics. Religion is of "pivotal importance" and Islam defines the characteristics of Tajik national identity.(pp.1115-1121) Regionalism, off-course, has been identified as a "a tacit constant" in all Central Asian republics (p.1126) along with ethnicity. There was a striking consistency in the percentages of votes polled by three leading political parties of Tazikistan viz. People's Democratic Party of Tajikistan (Hizbi Demokrati-Khalkii Tojikston), the Communist Party of Tazikistan and Islamic Renaissance Party of Tajikistan (Nahzati Islomi Tojikiston) in both 2000 and 2005 elections to the parliament.

In **Turkmenistan**, the Communist Party of Turkmenistan was re-christened as Democratic Party of Turkmenistan in 1991. A loyal opposition party, the Peasant Justice

Party was registered in 1992. An opposition group Unity or Agzybirlik aimed to establish multi-party system on Turkish model and was banned in 1990. It reemerged as Party for Democratic Development to be banned yet again. ([www.luptravel.com](http://www.luptravel.com)) Another anti-government group was People's Democratic Movement of Turkmenistan. ([www.gundogar.org/](http://www.gundogar.org/)) However, presently Turkmenistan is a single-party system with only one party, the Democratic Party of Turkmenistan.

In **Uzbekistan**, the Communist Party of the Workers of Uzbekistan supported equality and fraternity of all nationalities and religion, separation of the religion from the state and the school, acceptance of freedom of conscience, restoration of the socialist path of development, planned market economy, social protection of workers, mitigating social inequality and accepted reformed or "creatively developed Marxism" as its ideological foundations. It did not oppose the ruling People's Democratic Party of Uzbekistan, formerly the Communist Party, and talked of constructively criticizing it (Srivastava 1999:252-253). Other parties included "Adolat", government sponsored Social Democratic Party of Uzbekistan, "Istiklol Yoli" and banned "Birlik" (Unity), "Erk" (Will) and the Islamic Renaissance Parties. (pp.267-268) In 2005, however, prominent political parties according to the basis of election results were Uzbekistan Liberal Democratic Party, Uzbekistan Peoples Democratic Party, Self-Sacrifice National Democratic Party, Uzbekistan National Revival Democratic Party and Justice Social Democratic Party.

### **Kazakhstan, Kirgizstan and Tazikistan**

Central Asian nations had been a part of former Soviet Union and multi-party system has been a very recent phenomenon. Apart from communist, socialist, social-democratic,

liberal, nationalist, patriotic form of organizations, political parties and groups, there are political parties based on agrarian and working class issues. Politics and political parties and groups based on ethnicity, clan and religion too mark the contemporary political landscape of nascent Central Asian nations.

### **Concluding Remarks**

Political parties and policies of diverse ideological-political persuasions, ranging from liberal, social-democratic, socialist, communist or merely those subscribing to specific political identities and the programs based on them, exist in Central and South Asian countries. They represent numerous social, political, economic and cultural identifications like ethnicity, clan, region, religious, gender, language, national, class or caste, reflecting the diversity of this vast geographical area. These parties participate in the electoral processes in different countries, although a few of them are restricted in their legitimate activities, particularly in Central Asia, where party system is nascent and still evolving. An overwhelming majority of them, however, in both the Central and South Asia, function openly and actively, participating in the elections to the representative assemblies in their respective countries. Political parties, particularly in South Asian countries have undergone certain basic changes in their ideologies, policy-frameworks and approach to governance in the era of globalization.

However, one of the key problem that afflicts most of the political parties have been a sort of socio-political 'tribalism', whereby most of these do not have an effective and institutionalized method of internal democracy and elections to elect their leaders. A more centralized leadership tends to make political parties rather less responsive to their constituencies and other political groups and issues. Ironically, most of the political parties

that are considered to be the vehicles of political democracy in a party system are themselves not democratic as far as their structures and functioning is concerned. Many of these parties had displayed more democratic characteristics in their initial or formative years and have shown a tendency of ossification as they grew and consolidated with 'top-heavy' leadership.

Although there has been some justification about preserving the political and ideological characteristics of the parties lest they transform into some other political entity, however, this plea has in most cases been taken to extreme to justify dominance of the leaderships to the extent of curtailing inner-party democracy. Lack of inner-party democracy, an issue debated since the party system came into existence, has been the primary cause of disintegration of many political parties. Extreme situations had been witnessed in one-party or one-party dominant systems that came to become the core or axis of several parties and even political systems. Disintegration of such party systems resulted in substantial political trauma to such political systems and societies in the absence of a mature and responsive party system.

In an era of increasing democratization and globalization, such a structure of most political parties is becoming anachronistic vis a vis the growing complexity of politics in which newer social, economic, and political groups, identities and issues are increasingly becoming incorporated in the mainstream of the political activities compared with the past. Such political 'tribalism' has politically emaciated and marginalized many a political parties that were unable or unwilling to incorporate or adjust to such changes, that were particularly precipitated by increasing globalization and communication, effectively bringing about paradigmatic changes in local, regional, national and international political dynamics. Even 'advanced' and older

political democracies are afflicted with certain governance-related problems that have to do with the social and political culture inherited from a communitarian past. Leaderships of the political parties, once in the government, seem to abandon or undermine their role as the representatives of the society, their constituents and their interests and seem to increasingly rely on the permanent institutions of the State like the bureaucracy. Their primary role as the custodians of interests of the society gives way to the institutions of the State ruling by proxy.

In extreme forms, such situations are seen in authoritarianism and quasi-authoritarianism of elected regimes. In several cases this is due to ill-equipped politicians getting elected to the government and the resilience of the institutions of State coupled with a submissive political culture in the name of maintaining 'social harmony'. Another problem is that despite universal franchise, individual freedom and the private sphere of individuals are often violated in the name of so-called public good with impunity under the leadership of democratically elected politicians. That the individual and private spheres of individuals are sacrosanct and inviolable in a political democracy is not understood by many a political leadership.

There is few effective institutional mechanisms and norms to defend the private sphere of individual and provisions of penalty for violating them. This is primarily due to an incomplete understanding and persistence of a political culture that fails to accept that political democracy is much more than merely electoral democracy and electing governments. Political democracy is primarily about emancipating and protecting the individual from the excesses of the States, governments or organized groups and structures by encouraging a political culture of decentralized self-rule. A lack of

understanding reflects in the policies, laws and modes of governance in these nations and the avenues provided to defend such a meaning of political democracy.

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## Chinese Economic Transition

*Jamie Morgan*

### **Introduction**

In 2005 the People's Republic of China (PRC) became the fourth largest economy in the world. Goldman Sachs estimates that by 2041 the PRC will be the largest economy in the world (Wilson and Purashothaman 2003). On the basis of its own statistics, the PRC has maintained economic growth rates in excess of 7%, and usually greater than 10% for more than twenty years (NSBC 2006). The PRC has become increasingly significant in terms of global economics whilst also becoming, politically, a major global power for a number of reasons. It has become (a) a major location of global manufactures assembly; (b) a major source of demand for global resources; (c) a major source of consumption growth in the EU and USA, through its cheap exports; (d) a major holder of foreign currencies and gold (through its trade surpluses); and (e) a major destination for foreign direct investment (FDI).

However, in the 1970s, RAND (Pillsbury, 1975) and the influential US Council on Foreign Relations (CFR) were estimating GNP growth of no more than 5% per annum over fifteen years to 1990 whilst asserting that leadership change would leave this figure, and the economic model, unaffected (Whiting & Dernberger 1977). This did not change with the rehabilitation of Deng Xiaoping and his quasi-formal ascension to the leadership of the state and Party between 1977 and 1982. Moreover major innovators in our understanding of East Asian economies also held to the view that China was unlikely to change or grow significantly (Johnson 1982). As a "transition economy" the PRC therefore begs explanation. That explanation must account for the strategy of transition, and because that strategy confronts the

characteristics of a transition economy and of the PRC in particular, it must also address the nature of the problems that arise from those characteristics. But not only this, the very process of addressing those problems has created new ones for the PRC. In the following sections therefore I set out:

- The command economy and motives for change.
- The reform strategy.
- Early reform in the context of transition theory.
- Characteristic features of the relative success of Chinese reform.
- Emergent problems of reform in the 1990s.
- The perpetuation of problems into the twenty-first century.

Looking at China in these ways highlights just how precarious continued growth is and how that is becoming an increasing issue of global governance because potential sources of instability and crisis in and for China are increasingly sources of instability and crisis for the world. I address issues arising from this in the conclusion.

### **Command Economy and Change**

What has become known as the "reform" period in China is commonly dated from the third plenum of the Eleventh Central Committee in 1978. Reform focussed on a basic shift in economic orientation from a command-style economy to a mixed economy of state control and market incentives and competition. Setting out the basic characteristics of the Chinese command economy gives some idea of the scale and complexity of change.

The command economy was one where individual ministries at a national and provincial level broadly determined resource allocation, production growth targets and price and output levels (Harding 1987). These were administered through a system of large

rural communes, village-based farming collectives and urban state-owned industries, categorised as work units. The various forms of work unit were the primary providers of employment, welfare and services for the populous from cradle to grave (what became known as the “iron rice bowl”). Schools, hospitals, and housing were adjuncts of them. Labour was allocated to them, assigned a job and a grade, with commensurate (differential) pay and access to services. The system was highly bureaucratic, highly restrictive in terms of individual movements, geographically and occupationally, and with a strong degree of disciplining surveillance of individual behaviour (reinforced through local street committees). All capital and land effectively belonged to the state-Party (and according to the constitution to “the people”) and, especially after the early 1960s, there were no official markets or non-state outlets for any form of good or service. What one wore, where one lived, how one acted, how one worked, and what and how one consumed were highly determined.

Clearly changing such a system confronts the central problem of how to transist from its particular characteristics to different characteristics. Ultimately, this is not simply a matter of changing some small aspects of the economy because the system is an integrated social model. Substantively changing the system is a basic transformation of society. This is one reason why observers did not expect fundamental economic change. Engaging in it would be complex and difficult but also potentially unpredictable and perhaps dangerous in terms of political stability.

Change thus seemed like a high risk affair raising the initial orienting question, what could possibly motivate such change? A number of mutually implicating answers can be provided. China was manifestly a large and relatively poor nation albeit a politically significant one as a nuclear power within the

military-strategic context of the Cold War. However, relative poverty in isolation does not itself explain why change occurred when it did. It may be the case as Deng Xiaoping and others asserted that communism did not and should not mean poverty. But for the state and Party to undertake basic transformations in economic and social relations must entail a lack of confidence in those economic and social relations. This can be seen in several lights.

By the end of the 1970s there was a general and widespread cynicism concerning a focus on political consciousness as the primary mechanism for development of the state. This cynicism was a result of the rapid and fundamental changes in political line that had occurred since at least The Hundred Flowers movement of 1956. Each movement entailed basic changes in orientation to iconic personnel and also the historical narrative of the Party and state. Yet each “correction” remained in many ways unacknowledged and it is significant that the Party resisted writing an official history precisely because of its Orwellian approach to its own past. Moreover, each movement and reversal had its specific victims (sentenced to various forms of re-education through labour and imprisonment) but also broader corrosive effects on individual human relations and trust in the public sphere. It is from this perspective that some authors have argued that the Party opted to shift its political strategy to that of a “performance regime” (Zhao 2001), focussed on delivering increases in material well being.

The concept of a performance regime is a useful one because if we think of the central task as one of securing ends with no prior sense of a total and clear commitment to specific means then the policy of change does not necessarily immediately confront the fact that change can and probably will become a matter of fundamentals of the system. Nor

does strategy need to be clearly defined in terms of a telos that is tied to a particular economic model even though we can look at the way society, the economy, and the state have changed and retrospectively see that it is a transformation shaped by policy, but a transformation not necessarily fully conceived at the outset.

One can consider motives for adopting a performance regime in a variety of ways. One can look at it as a form of pragmatism by the Party—as a means to perpetuate Party control—something simply not anticipated by those analysing China in the 1970s. But one can also look at it as a genuine commitment to produce positive change in the PRC. The two are not incompatible if the proponents see the Party as the best vehicle for that change and economic change as necessary in order to deliver material improvements.

Notably, many of the key early figures in reform were victims of the system as well as powerful figures within it. Many of them were veterans of the Long March (1934-1935), the war with Japan (1937-1945) and the civil war (1946-1949) with a living experience of the poor conditions in China before and during the wars. These figures encapsulate a personal narrative that is more than an instrumental drive to power. It also seems to speak to a sense that general conditions ought to be improved as an original motive for that drive because, for many of them, this had been their original motivation as revolutionaries.

That commitment also extended to external security and a sense that China should be an important nation within the world. After the Sino-Soviet split of 1959-1960 relations with the USSR had remained relatively poor. In 1979, a USSR-backed Vietnam toppled the Chinese-backed Khmer Rouge regime in Cambodia. Fearing encirclement, China invaded Vietnam. China's rapid defeat highlighted the

antiquated nature of their military technology and strategy ("peoples' war") leading to a strong sense that investment was needed to modernise the armed forces. Increased investment implies either a steady increase in the proportion of GDP expended on the military or an absolute increase in GDP through economic growth. In the long term the latter is not only the most viable option, it is also, as the negative experience of North Korea has subsequently shown, the only one compatible with a performance regime.

What these points suggest is that the decision to reform the economy may not have been either as risky or inexplicable as it may have seemed from a narrower standpoint. This is particularly so when one considers that the period was not just one where there were reasons for change within China but also an international context that was becoming conducive to such change (O'Leary 1980). China's diplomatic relations with the USA were normalised in 1979. The USA's relations with the USSR deteriorated with the invasion of Afghanistan and the election of Reagan. East Asia was increasingly becoming a region of investment and economic dynamism as Japan, South Korea, Taiwan, and Hong Kong expanded. As such there were good diplomatic-strategic and economic reasons for the USA and key regional states to encourage Chinese reform. Deng visited both the USA and Japan in 1979 and was feted in both.

## **Reform Strategy**

As various commentators noted of the early phase of reform in the late 1970s and through the 1980s (White 1993, Nolan 1995) China's reform strategy was incremental, experimental and localised. Possible policies were tried out in specific regions and provinces, adjusted on the basis of the experience, discarded if problematic and gradually applied nationally if seen as viable.

The state began with what it identified as the easiest forms of reform, ones that would have an immediate impact, would be publicly popular, and had no obvious losers. Thus they began by introducing (1978-1983) various rural-agricultural reforms, giving the peasantry control over small plots of land to produce crops in addition to their state quotas. State quotas were also contracted out to what had previously been village-wide production teams within larger collectives. Farmers were empowered to sell their produce at locally created markets, producing a profit motive for the farmers and variety and choice for local township workers. This model was extended at the time to the production of small goods and services in local collectives with access to state funding, subsequently termed township village enterprises (TVEs) and the combination began the process of creating local market economies with a concomitant reinvigoration of the money economy.

In keeping with this localised experimentation policy, the state also created (1979) some initial coastal Special Economic Zones (SEZ) in which it provided a modern infrastructure and a (relatively) skilled labour force and in which foreign direct investment in joint venture businesses could be encouraged through preferential taxes. The SEZ provided a location for additional experimentation in organizational, labour and market reform, as well as a source of skill and technology transfer and revenue from exports.

The state then used this experience to experiment with new organizational models for the large and medium state owned industries (1984, though particularly after 1986). Gradually, management was given greater autonomy, in some cases enterprises were “leased” to management or worker collectives and state grants were replaced by state-bank loans. A greater recruitment emphasis was placed on technical and organizational skills than political reliability

(“redness”), and some profit retention was introduced, as were various pay incentives for workers. New workers, employed on a new contract basis, could also be hired and fired, beginning the dissolution of the iron rice bowl system. The flipside of this was that workers could also apply for jobs, refuse assignments offered by the state labour bureau, or opt to leave the state sector entirely and go into some other form of employment. As such the beginnings of a mixed economy system with a focus on motivating quality improvements, productivity gains and with a commensurate focus on creating a labour market, with some if limited degree of mobility, began to emerge within localised experimentation.

### **Early Reform and Transition Theory—A Tacit Chinese Exceptionalism**

By the end of the 1980s the economy of the PRC had undergone significant change. The number of industrial products subject to mandatory planning had reduced from a height of 500 to 60 and the number of agricultural commodities to zero (Harding 1987:109). This did not mean that the economy was either unregulated or privatised, the majority of capital remained in state and in collective hands, and economic activity remained highly bureaucratic. The state continued to provide a welfare system through the work units and continued to set or regulate key prices (rents, strategic foodstuffs, fuel). Over 40% of output was still subject to detailed control under a five-year plan system.

Change thus remained partial and incremental. This is a significant point because the collapse of the communist states in Eastern Europe in 1989 and then of the Soviet Union in 1991 created a new discourse within developmental economics focussed on the wholesale reform of former communist command economies. The dominant form of this transition theory and the one most

strongly advocated was termed the “Big Leap” strategy. This approach was most closely associated with the work of Sachs and of Kornai (for analysis see Nolan 1995). It argues that a command economy and a market economy are so fundamentally different that a slow process of transition from one to the other will create two catastrophic problems. First, they argued that there is no clearly definable halfway house between, on the one side, state control and state ownership and, on the other side, private property rights and functioning capital, product and labour markets. To move slowly from one to the other would, therefore, simply create instability and confusion in a way conducive to massive corruption and social conflict as resources constantly and competitively shifted in use, ownership and meaning. Second, delays in the process would create the conditions for further inertia as vested interests within the political system would mobilise to further retard the process of transition. In combination these two points led to the assertion that the slower the process of transition the more painful it would be in the long-term and the more “distorted” the outcome i.e. the further from a viable, dynamic competitive market economy would be the result. Therefore, according to the Big Leap strategy the logical approach is to transform ownership, control, and regulation in all facets of the economy in one phase of radical change.

Clearly, China had not followed such a policy and had experienced relatively high economic growth in the 1980s. It had also remained relatively politically stable despite the suppression of the democracy movement, focussed on Tiananmen Square in 1989, which resulted in an arms embargo and general international condemnation. In contrast, following to a greater or lesser degree forms of the Big Leap strategy in the early to mid-1990s, Eastern Europe and many

of the former Soviet Union states suffered massive deindustrialisation, huge social dislocation, unemployment, intermittent periods of negative economic growth, widespread bureaucratic corruption in the form of private capture of publicly owned assets, particularly natural resources, and a deep crisis of the welfare system. This raises the question, why the Chinese experience, at this stage, had not been more strongly identified as transferable?

One possible reason is that the early 1990s was characterised by the dominance of a view captured by Fukuyama’s “End of Ideology” thesis (1992). According to this view there is no viable political alternative to the democratic state in the world of ideas. Forms of authoritarianism and totalitarianism, with which the very concept of a socialist or communist state was by now conflated, were no longer tenable or justifiable and would necessarily be replaced where they still existed, as they did in China. A key component in the democratic form of state and, in democratisation discourses of the time, a possible source of its constitution, was a dynamic market economy. Since the emergence of this argument came in the wake of the re-emergence in the late 1970s of variants of classical economics a dynamic market economy tended to be associated or conflated with the dominant form of economic theory and related policy forms.

Unlike the Chinese case, the Big Leap thesis encapsulated a strong sense of both specific means and substantive telos, because these were built into the underlying assumptions of the economics. The market models (to which the Leap aspired) were based on highly mathematical constructs of equilibrating market clearance with deep roots in the conceptual framework of demand and supply analysis. The well documented lack of regard for historical, cultural, and institutional factors in the variance in real

economies, and the curious lack of real time analysis in the mathematical models, may be one reason why, on paper, the economics served to foster a sense of the plausibility of a Big Leap strategy. Furthermore, a policy push for the Big Leap strategy also made sense in terms of Europe and the USA's interest in access to markets, capital and resources and this policy push was expressed in various quasi-official outlets such as *OECD Economic Studies* and *Economic Policy: A European Forum* and *IMF Survey*.

Another possible reason why the Chinese experience was not widely heralded as transferable might be a sense of Chinese, and more generally, East Asian, exceptionalism. Through the late 1980s, early 1990s and prior to the East Asian financial crisis of 1997, economists and global economic institutions such as the World Bank and IMF were still trying to come to terms with the East Asian "economic miracle". Economic growth in East Asia did not fit with the policy advice of the "Washington consensus" or with the broadly neoclassical economic models that the consensus was rooted in. This was a source of conflict between East Asian states and the institutions concerning how their developmental models were to be represented and accounted for. The global institutions attempted to accommodate the East Asian development models to their own perspective. Where this seemed to be problematic there was a tendency to "other" an East Asian model in highly general terms as "Confucian capitalism". The result was a tension between what Said refers to as "Orientalism" (1978) or the false cultural reification of "the East" by "the West" and what Dirlik refers to as "self-Orientalism" (1995) or a responsive false cultural reification of "the East" by its more authoritarian leaders. This tension was defined in terms of claims of exceptionalism that then spread across issues of the universality and transferability of political

systems (individualism and democracy versus the collective and authority), human rights (individual versus group, economic versus political), and economic models.

In many respects, China in the 1980s and 1990s was to become one more East Asian state subject to this process of exceptionalism. In a 1985 report the World Bank stated, "The lessons of international experience are often ambiguous and controversial. In any event, they are hard to apply to China, a country that in important respects differs from all others and is not easy for outsiders to understand." (World Bank 1985:1). In a 1992 country study, however, the World Bank clearly identified experimentation etc. as key aspects of China's reform strategy and noted that many aspects of it might be "adaptable" (World Bank 1992:xv-i). Yet the World Bank's most important comparative study on transition economies, *The World Development Report 1996: From Plan to Market*, despite a number of caveats comes down on the side of "strong liberalization" and "privatization" in markets based on "rapid structural and institutional reform" (World Bank 1996:6). Subsequent studies have continued to acknowledge the effectiveness of China's reform strategy (World Bank 1997a:8-9), whilst continuing to analyse its economy using problematic models such as general equilibrium theory (World Bank 1997b:16) and total factor productivity. The combination has tended to result in conclusions based on the presumption that the Chinese economy will not just become marketised but that a market is adequately represented by such models. This itself has become controversial as the economic theory itself and the Washington consensus have increasingly been criticised in recent years. More significantly, perhaps, the issue of transferability has faded in the literature – principally because most of the

states to which it might apply have already undertaken structural reform.

It is important to note in this context that criticism of the way that the Chinese case failed to be generalised does not mean that aspects of the Chinese reform situation were not specific to it. That there can be specific aspects is of course precisely an endorsement that different economies have different historical and political (international) contexts and characteristic features, some of which manifest variations in cultural, institutional and social relational elements. These can be real rather than simply a form of Orientalism that emerges because of the contradictions of an economic perspective that cannot adequately deal with history, culture etc. Exceptionalism served as an exclusion that reinforced a Big Leap approach in opposition to the more basic point that difference is a significant aspect of any real economy.

### **Characteristic Features of Success**

In addition to the basic strategy of reform followed in China, the characteristic features of Chinese reform and its context that have contributed to its relative long running success in comparison to Eastern Europe and the USSR range from prosaic idiosyncrasies of demography and geography to accidents of history and its relation to the specifics of cultural ties, to matters of global geo-strategy. These include:

- That over 70% of the population were initially rural and predominantly worked in large state-sector collective agriculture that had been severely disrupted by the Cultural Revolution. Great gains could, therefore, be made simply by disaggregating land use, enabling intensive and extensive growth potential to be developed without radical shifts in ownership, without the initial widespread disruption to the social system that large-scale migrant urbanisation would require, and without the need for sudden and

massive improvements in capital investment and infrastructure that rapid urbanisation as a means to the transfer of labour as a factor of production would entail.

- Because the Chinese economy had remained predominantly agriculturally and rurally based, with a proportionately low urban population and level of industrialisation, the planning structure of the original command economy prior to reform had remained, compared to the USSR, relatively narrow in terms of the total range of items covered, more flexible in its production targets and planned output levels, and, crucially, more decentralised (especially in agriculture). Although a highly bureaucratic system it was one with a lesser degree of inertia than other command economies, and was thus easier to change, particularly through an incremental policy process. There was, therefore, less scope for ministerial vested interests in the planning system to impede change from below.

- Where resistance did occur in the planning system it was based around personnel promoted during the Cultural Revolution on the basis of their radical political credentials and who feared for their status now that its victims were returned to power. Resistance, therefore, served to identify precisely those who lacked technical competency and who could be progressively replaced by a new generation of skilled labour as the education system recovered after the Cultural Revolution.

The most significant constraint on rapid change in the planning system was less about vested interests from below and more about competing opinion concerning the pace and extent of that change within the upper echelons of the Party. The incremental and experimental approach persisted partly because of that debate. Debate itself was now more acceptable because there was a conscious effort to change the stakes of

political struggle within the Politburo and Central Committee away from life or death decisions about conformity to the whim of a charismatic leader. Chen Yun, the main economic architect of the post Great Leap Forward reliance on small agricultural markets in 1960-1963 to deal with the famine the Leap created, argued in the 1980s for slow reform where markets would always be a supplement to a majority planning system (birdcage theory). Others within the Politburo argued for a more rapid extension of a majority marketisation. Since, all sides were committed to some markets there was a degree of consensus. However, contrary to the Big Leap thesis, a degree of dissent within the political elite proved fruitful. The idea of fuller marketisation did not become dominant until Deng Xiaoping's concept of the "socialist market economy" as part of "socialism with Chinese characteristics" was endorsed by the 14<sup>th</sup> Congress of the CCP and by the Politburo Standing Committee in 1992, almost a decade and a half after reform began.

- From an early stage in reform, the state was able to mobilise labour, particularly in the SEZ, in an oppressively disciplined but economically highly effective way through the use of quasi-militarised production regimes. Typically young, female and "docile" labour was recruited in a controlled rural-urban transfer to barrack-style factory compounds. Intensive production was introduced that utilised some practices and systems from mass movement political campaigns and exploited the legacy of the highly regularised personal conduct typical of socialisation within the former system. In 1993, the People's Liberation Army (PLA) operated 20,000 economic enterprises. Even though the PLA's role in private enterprise was subsequently reduced and then formally eliminated, this production regime has continued to prove attractive to domestic

business and "joint venture" multinationals in China.

- The PRC benefited greatly from relations with Hong Kong and Taiwan. The PRC was able to exploit the cultural-historical ties of this "Greater China" to create a mutually beneficial economic bloc. Key SEZ were created in Guangdong and Fujian provinces in close geographical proximity to Hong Kong and Taiwan providing cheap labour and tax breaks to overseas producers whose domestic costs had been greatly increased by more than a decade of economic growth in the NIEs. Hong Kong served as a relay point for Taiwanese reinvestment avoiding direct political conflict between the antagonistic governments of the PRC and Taiwan. It also served as a key port for re-export and, thanks to the British development of its capital markets, as a site for finance. Hong Kong thus provided a mature capitalist centre whilst Shanghai was developed through the 1990s.

- The large overseas Chinese (*huaqiao*) business community provided an initial source of FDI and of transferable business skills and technology that allowed the SEZ policy to succeed. Although Japan, the USA and the EU had good economic and geo-strategic reasons to invest in China, until the late 1990s their combined FDI constituted less than 30% of the PRC total, compared to the 50-65% that was directed from and through Hong Kong. Notably, the USSR and Eastern Europe simply lacked this kind of cultural resource.

An important point that emerges from these characteristics and from the form of economic strategy that those characteristics both operated in conjunction with and helped to facilitate is that to a large degree the reasons for the relative success of the PRC in its transition from a command economy to a globally significant mixed economy are specific to the PRC. Though one could argue



that Eastern Europe and the USSR might have avoided catastrophic economic dislocation by adopting the PRC strategy and by rejecting the Big Leap, one could not necessarily conclude that this would have created commensurate levels of growth. One can make a similar point regarding the South East Asian states that have more recently begun a process of transition - Vietnam, Laos and Cambodia.

States like Czech and Poland have more recently been able to take advantage of their geographical proximity to key industrial areas in Western Europe to develop through the relocation of European manufacturing, such as car manufacture. Vietnam, Laos and Cambodia may be able to take advantage of low labour costs in order to take advantage of new production system relations for some economic sectors of the kind explored by Klein's *No Logo*. But neither set of states has had the large rural population, or access to the cultural and financial resources of the PRC.

Russia, has similar geo-strategic significance to the PRC and one might think that it ought to be able to command a similar long term leverage for continued access to key markets in Europe and America for exports. However, unlike the PRC it did not pursue a policy of creating an export dependency in those markets that fostered continued access and thus continued growth.

Prior to its admission to the World Trade Organization (WTO) in December 2001, the US government required that China's market access be reconfirmed on an annual basis. Despite its poor human rights record, however, and issues over intellectual property rights created by widespread piracy in the PRC, the awarding of this Most Favoured Nation (MFN) status tended to be a virtual formality for two reasons. First, both the Bush and Clinton administrations pursued forms of "constructive engagement" diplomacy with China. This was based on the thesis that

increased economic interdependence would moderate China's geo-strategic threat and, in the long-term lead to some form of democratisation. One can think of this as the pro-active diplomatic analogue of Fukuyama's *End of History* thesis. Second, a powerful business lobby emerged to press for MFN. Companies like Toys-R-Us, and later, Walmart, became highly dependent on cheap Chinese manufactures often ordered and contracted in timeframes that did not overlap with the MFN renewal period. The denial of MFN would seriously disrupt supply forcing high cost substitutions, raising prices and reducing profit margins. Since higher prices would also mean lower real disposable incomes for US consumers, the appeal of the concept of "constructive engagement" cannot be seen as entirely independent of this economic pressure. This kind of access leverage has continued to the present day.

### **Emergent Problems of Reform in the 1990s**

Though it is important to make the point that in many respects the bases of China's economic achievements are specific this by no means lends credence to the Big Leap strategy when one considers the Leap's catastrophic effects on real economies but it does indicate that one cannot transist from one social model to another without some degree of difficulty. China may have avoided the fundamental dislocations experienced by states that opted for the Big Leap strategy, but it has experienced many of the same problems to a lesser extent, some further problems related to China's specific characteristics and also some additional problems created by the incremental nature of its reforms. This tends to indicate that the very strengths of the PRC reform strategy can also be viewed as vulnerabilities. The core of many of these vulnerabilities has been that, beyond relatively ambiguous statements concerning overall ideological frameworks, such as the

socialist market economy, the nature of Chinese transition relied on an absence of detailed unified concepts of specific ends which has translated into a general lack of key policy formulations that would anticipate and forestall some of the problems that transition itself creates.

The initial focus on agricultural reform allowed rapid growth without commensurate rapid urbanization or development of a national infrastructure. However, income growth produced consumption growth, as intended by the performance regime strategy, and this in turn has produced a greater demand for an effective national power generation structure. The growth of Township Village Enterprises (TVEs) in the late 1980s and early 1990s (which tailed off sharply in the late 1990s) exacerbated this demand in rural areas and the expansion of FDI and joint ventures has exacerbated it in urban coastal areas. The result has been a widespread growth in power shortages in the 1990s and demands for an integrated national policy (Xu 2002). Similar problems have emerged with the transport infrastructure which has been overloaded by the increased movement of goods and people.

- The option for labour to leave the collectives and work units gradually created a growing “floating population” of economic migrants whose size has grown from 50 to 200 million over the 1990s. This population constitutes a new temporary labour pool and transient hidden unemployment problem, much of it seasonal created by peasant farmer migration during annual farming lulls.

- Since welfare and service provision were focussed around collectives and work units, the growth of work (and a floating population) outside of them has created a problem of non-access to services. Furthermore, the gradual shift away from the work unit system has created a long term need for a fundamental restructuring of the welfare

system that local experimentation and incrementalism has not easily addressed (Chow, 2000).

- The gradual reduction in control of production as TVEs and rural markets expanded, SOEs were leased, foreign joint ventures emerged, and labour began to earn and expend income in new ways has created the need for an effective fiscal policy based on taxation systems that the former model simply did not require. Implementing such a system and ensuring compliance has proved complex—requiring for example, a new technically competent cohort of tax inspectors and of trained accountants, as well as an understanding of the system within business and society. The problem of creating a tax system meant that the state remained reliant on SOEs and former SOEs for the generation of tax revenues because these tended to be the largest enterprises and one’s concerning which it had the greatest degree of control and data.

- Implementing reforms in SOEs created a number of subsequent problems and dilemmas. The SOEs and particularly the management within leased SOEs found themselves commanding powerful influence in their relations with the state-owned banks because the SOEs remained large urban employers even though their significance in production terms was reducing (by 1992 the non-state sector already produced 47% of China’s total industrial output; Zhang 1996: 215). Leasing gave control of the massive capital assets constituted by the SOEs to management who could use this as leverage to gain access to additional capital. As of 1992 SOEs could also become joint stock companies where shares were issued that could only be bought by managers and workers. The SOE would appear to be (collectively privatised) however, if the capital raised by the share issue ran out the SOE could still call on the state. The state

consistently resisted implementing bankruptcy regulations on the SOEs and “former” SOEs. During the 1990s, many of them therefore, faced a “soft budget constraint” which translated into a rolling accumulation of low interest rate loans and capital transfers affecting the real solvency of the banks and creating an ever-expanding source of state debt. Much of this was hidden for two reasons. First, many of the SOEs now appeared to be private or quasi-private and thus self-sustaining, but the fiscal basis of the state required tax revenues from the SOEs and this resulted in creative accounting where the state would allow SOEs, and “former” SOEs to report notional revenues and profits based on projections or unfulfilled orders and contracts or capital transfers, mainly through the state banks, which could then be recycled back into the state through taxation. Second, the collective sector, such as the TVEs, could also access state funding through the banks creating the same problem. In order to access funding collectives would report output and future output that may be unrealised. Since the system remained highly bureaucratic and the careers of cadres within local government and state ministries may rely on delivering good growth figures over-reporting became a systematic tendency.

- Emerging tensions created by the relation between the banks, the SOEs and the role of cadres in reporting growth figures manifested increasing opportunities for forms of corruption. SOE management could use capital access to fund lavish lifestyles, bank officials and other state cadres received gifts to facilitate a process that their own interests in reporting good growth figures in any case supported. Moreover, the disaggregated nature of the original planning structure of the command economy not only facilitated change but also provided an opportunity for bureaucrats to profit from it. Since the economic system remained highly regulated,

many Party cadres and state officials were able to use their positions to enable some businesses and block others. Many officials either set up their own businesses or became consultants or part-time employees of businesses. Corrupt practices have increasingly become socially corrosive.

- Rapid geographically differentiated growth combined with infrastructure limitations and competition for limited resources created intermittent problems of inflation, running as high as 30% in certain urban areas in the 1990s. Since much of this inflation has increasingly been outside of the planning system controlling it has required the development of a new set of less direct macro-economic levers and policies that can address the differentiations of the system. This in turn has required a debate over the nature of effective macro-economic policy (Keynesian, classical or monetarist—Liu and Liu 1999) and also the creation of a reliable data collection and collation system, as well as a policy administration for effective implementation. Inflation has thus created new problems of control as well new problems for the economic system associated with real prices, incomes and wages. Where inflation occurs it has tended to increase inequalities and thus social divisions contributing a two-tier economy and society.

- In the 1990s it was estimated that China had approximately 7% of the world’s arable land with which to feed 22% of its total population. As a country with a large population it has always faced a precarious situation in terms of self-sufficient food production and water conservation. However, cumulative economic growth has exacerbated this situation and added to a growing set of problems of environmental sustainability. A heavy reliance on coal for domestic heating and for electricity production has produced a large greenhouse gas emissions problem, which is now being exacerbated by increasing

use of energy and of fossil fuels for new consumption goods. Industrialisation in the 1990s began to reduce the amount of available arable land as well as causing widespread deforestation. Pollution has begun to affect the health of the population and the viability of water resources.

What is significant about these problems that came to the fore in the 1990s is that many of them are ongoing. They are complex and interdependent problems created by the nature of change. They are in many respects cumulative issues because the ongoing process of change has ultimately transformed the basis of the total social model that was the PRC of the pre-reform era. Incrementalism, experimentation etc. have been successful in creating growth but by their very nature they do not entail a clear vision of what the new social model will look like. The PRC may therefore have avoided the experiences of the other transition economies in the early 1990s, precisely by lacking a commitment to dubiously specific means and ends concerning transition, but it is not certain that the consequence of this has been the creation of a sustainable and stable alternative form of transition to a form of capitalist mixed economy combined with an effective civil society, and viable polity.

### **Twenty-first Century Issues**

As economic growth has continued it has created a number of problems. Differentials in the distribution of material gains from growth have created new social cleavages. Growth itself has created problems of sustainability in terms of both environmental degradation and of resource acquisition, contributing to global issues over energy and resource security. Furthermore, the nature of the political system has meant that transition has not just lacked a unified policy solution but has so far proved systemically unable to address the sources of discontent embodied in new social

cleavages. Part of the problem is that a performance regime must maintain economic growth but doing so does not guarantee that growth delivers benefits. This is a systemic problem of the social and economic structuring of growth. Moreover, that structuring has increasingly reflected the power hierarchies of the broadly neo-liberal economic order into which the PRC has integrated, despite the fact the PRC did not begin from (and does not now avow) a reform strategy based in the free market economics that underpin neo-liberalism.

### *Rural Issues*

Although the first to benefit from the reform period, the PRC's rural population, especially in the West, are increasingly being left behind (Riskin et al. 2001). Steady increases in labour mobility and migration have reduced the rural population to 58% in 2005. This is still comparatively high. Average per capita rural income in 2005 was £232 compared with £750 in urban areas. Since joining the WTO, exposure to low world food prices has reduced China's farmers' real incomes at the same time as urban incomes continue to grow more rapidly. This differential has been exacerbated by unemployment in the TVEs and the empowerment of rural officials to levy local taxes and requisition land for development. Arbitrary one-off local taxes in the early 2000s to fund local development projects and the compulsory purchase of land have created a growing rural-based unrest.

In 2005 there were 87,000 recorded protests in China, the majority of them rural. The annual number of protests has been increasing year on year since the mid-1990s. In 2005 Hu Jintao, who replaced Jiang Zemin as leader of the Party in 2002, called for a "new socialist countryside" and at the 2006 National People's Congress, Premier Wen Jiabao used his opening address to identify the rural-urban divide as a central issue.

However, though the Party and state's response has been to publicly acknowledge growing social division and commit itself to addressing it there seems to be definite limits to how far they can do so. If they are to maintain compliance with WTO regulations they can have little control over imported food prices and thus little control over a fall in the terms of trade under which the PRC's farmers operate. Rural-urban income inequality is therefore liable to continue to grow. Given that over 600 million of the population are still rurally based, some form of wide-scale income subsidy seems unlikely on the basis of cost. In any case, a great deal of land requisition is for infrastructure and industrial projects. The state needs such projects to meet the power generation demands of industrialisation and of consumption. Industrialisation is needed to maintain the basis of the performance regime. Though the state can to some degree address problems like compensation it has little interest in halting compulsory purchase and dissent therefore seems likely to grow.

### *The Demand for Resources*

The PRC's degree of control in addressing environmental issues is highly constrained. According to the UN, 70% of the Chinese population is likely to be urban by 2050. According to the *European Commission Environment Research Programme*, China aims to build 300 new cities by 2010 to meet the demands of population growth and labour migration. In the mid-1990s China began to develop its hydroelectric potential, introduced new environmental laws to curb industrial waste problems, and committed itself to spending 0.8% of GDP on conservation. However, in the latter two cases, enforcement has proved difficult precisely because of the decentralised nature of reform and the ability of local bureaucrats to facilitate non-compliance with both environmental and

health and safety standards to boost short-term profits. A 2004 report by the State Environmental Protection Agency found that most regions were already failing to meet existing targets and that many of the hundreds of approved conservation projects in the previous five years had yet to begin construction or implementation.

Part of the problem is that industrialisation has created a huge demand for raw materials and thereby increased the production of wastes and emissions. In 2005 the PRC was the world's largest consumer of copper, zinc, tin, rubber, cotton, wheat, rice and cement (Worldwatch 2006). In 2004 it was the world's second largest consumer of oil and accounted for 26% of total consumption of steel and 34 ½ % of coal. The result has been a decline in air quality, a rise in desertification and the poisoning of arable land, a fall in water levels and water quality, and a problem of acid rain.

*China's Global Resource Acquisition Strategy*  
Meeting the resource acquisition challenge has resulted in further potential environmental problems, political conflict, geo-strategic concerns, and exacerbated human rights violations in unstable areas of the world. The PRC has pursued improved diplomatic and economic relations with African nations that have large oil, gas and mineral resources. China's massive oil investment and arms sales have been key components in maintaining the Sudanese Islamic regime and by association, the oppression in Darfur. The PRC state oil company CNOOC and its sister companies Sinopec and PetroChina have also pursued a policy of acquiring drilling fields, firms and rights in Central Asia. In March 2006, President Putin and Hu Jintao, provisionally agreed a pipeline project, intended to supply 1.6 million barrels per day from the main Siberian oil hub at Angarsk in Eastern Siberia, to China's main oil refinery

centres in Daqing. Such resource issues may be serving to facilitate the restructuring of global security complexes. In 2005 Russia and China engaged in joint military exercises for the first time, and have also begun to coordinate their responses to US diplomatic initiatives within the UN Security Council, most recently over Iran.

Resource competition has begun to exacerbate historical antipathies between China and Japan. The PRC is embroiled in ongoing conflict with Japan over ownership of the Senkaku/Diaoyu Islands in the East China Sea. The islands are at the centre of large oil and gas deposits that both wish to exploit. CNOOC is already developing the Chungxiao gas basin which juts into territorial waters disputed between the two nations.

Most importantly, the PRC's resource strategy is no clear solution to its own environmental problems because it is not about sustainability in the environmental sense, but rather serving the needs of continued growth. As such, the global dynamics of its resource strategy are perfectly compatible with and may even facilitate continued environmental degradation at home, in turn fuelling dissent.

### *Failing Health Reform*

Environmental degradation is both a rural and an urban issue and has contributed to pressure on the Chinese health system at a time when the system is chronically underfunded and caught within the transfer of responsibility for welfare provision implicit in the shift from a command economy. The WHO ranks China as the fourth worst country in the world for fair allocation of medical resources. Official policy is to combine privately funded hospitals with state-planned low cost urban hospitals and universal health insurance by 2010. This seems set to create a two tier health system similar in form to the US—commonly considered the most

inequitable system amongst wealthy nations. In the meantime, the WHO has reported widespread problems in the Chinese health system that can only exacerbate discontent. In order to offset under-funding by the state over-prescribing and unnecessary testing have resulted in systematic overcharging.

### *Limits of Political Reform*

If the pre-reform system in the PRC suffered from a cynicism regarding mass movement political campaigns, social change has produced a new kind of cynicism based on scepticism regarding the state's underlying commitment to effectively combat growing inequality and social cleavage. This is both a result of the nature of transition (a lack of a sense of unified policy exacerbated by contradictory goals) and of circumstance (a decentralised system facilitating graft that helps to meet some of those goals). One of the claimed advantages of a performance regime strategy is that it focuses the population on material goals and as such reduces critique of the political system but increasing inequality and social cleavage have destabilised the capacity of the state to distribute material benefits to effectively meet the goals by which a performance regime is justified.

This in turn has created the need for an additional strategy from the Party to re-root itself in a rapidly changing society. There has been some (highly relative) progress in the political system in the sense that leadership transition has become more stable, politics is increasingly rooted in institutional structures rather than client-patron relations and hidden factional struggles only, the lowest levels of representation within the state are now based on elections, the party and state have withdrawn from large areas of private life, the rule of law has (to some extent) been introduced, and the legislative National People's Congress has become more active.

Furthermore, the Party has attempted to expand and restructure its membership to internalise and accommodate newly emerging and potentially powerful elements within society. In 2000 Jiang Zemin introduced the concept of the “Three Represents”—the Party’s role should be to promote advanced Chinese culture (limiting the corrosive social effects of Western consumerism) advanced social productive forces (capitalists) and the fundamental interests of the majority of the people. In 2002 on the eve of his designated retirement as General Secretary at the 16<sup>th</sup> Congress, Jiang succeeded in having his “Three Represents” raised to the status of Party doctrine. This occurred in the wake of the 1992 Party Constitution amendment that class struggle was no longer the central problem for society (and that socialism now meant “common prosperity”) which had provided the basis for the Party to begin to broaden its political coverage by establishing Party branches in private and foreign owned enterprises. By 2003 Party membership had also been expanded, reaching 67 million and 8% of university students (likely to secure employment in the private sector) were members.

These policies are aimed at social stability by legitimating changes that Party economic policy set in motion. However, when the Party fosters and legitimises changes within society this need not have the reverse effect of legitimising the Party. The leadership continues to fear the very social forces that its own policies have created: increasing personal autonomy, individualism, consumerism, self-expression. In strictly ideological terms they are antithetical to the notion of a vanguard Party. More importantly, acknowledging them steadily reduces the scope of the Party to one of fostering the economy and of a vague nationalism-culturalism. The very process of legitimating them fosters a narrowing of the performance

regime concept to an even more starkly functional one – what has the Party, what has the state done for me? This can only feed critique in the long term especially since it is a tendency the Party appears aware of and conflicted by—resulting in a mix of liberalism and harsh oppression which undermines a sense of the impartiality of the law and the inviolable nature of the private sphere. As such, much of the process of accommodation to the newly emergent society is one of policies that do *not* reroot the Party within it. They are policies of withdrawal or they are policies that show in stark relief how different the formal nature of the Party is from the society it “leads”.

Broadening the representation of the Party by recruiting students, new white collar workers, management and business is not the same as improving the legitimacy of the Party. This is because joining the Party need not entail any notion that there is a central core of coherent ideas that one need be committed to. The very notion that peasant farmers, workers, management and business can be members of the same Party tends to imply that such a core must be dissolved. Peasants, workers, management and business all have a vested interest in continued growth and thus a vested interest in being represented within the seat of power that ultimately commands the state. But they have different interests in the distribution of gains from growth and it is debatable that the Party can accommodate this level of interest for all.

In any case, enhancing legitimacy also entails some idea that the Party can and will effectively address the causes of dissent i.e. that legitimacy implies accountability and responsiveness. This raises the issue of what constrains the overall shape of policies and how this affects the accountability and responsiveness of the Party. In a performance regime this is centrally an issue of how growth is structured, this in turn is

fundamentally an issue of what transition has been from and to

### *Problems of the Imperative for Growth*

Population growth and increased life expectancy have increased the absolute number of dependents in China. Population growth has also increased the absolute size of the working age population. Both result in the need for economic growth to provide for increased employment and wealth over and above the new consumption aspirations that are built into a performance regime. The state estimates that it requires a minimum of 7% annual growth to maintain “social stability”.

However, since growth is occurring at the same time as restructuring of the SOEs, the fostering of flexible labour markets to encourage people to move into new employment sectors, and at a time of increasing rural-urban migration, employment insecurity and unemployment can and do coexist with economic growth. Total employment in the state sector fell from 110 million in 1997 to 76.5 million in 2001 and 67 million in 2004 (NSBC 2005) and has continued to fall thereafter. The Research Office of the State Council put the floating rural population at 200 million in March 2006 (CLBb 2006). This situation coexists with labour shortages in some sectors and regions. There is a shortage of assembly workers in manufacturing in the key SEZ because inflation and housing shortages have made it both expensive and difficult for low end migrant labour to locate there—floating does not therefore mean a problem solving flow of labour. Local younger and more educated labour has now begun to shift into the service sector in the key SEZ where pay, terms and conditions are better and here there is also a shortage. What this suggests is that poor pay has become a geographically relative issue of variable living costs as part of a labour market that has structural frictions that the simple

idea of flexible hiring and firing from SOEs simply does not address. In 1998 the reemployment rate of laid off SOE workers was 50% and this had reduced to 10% in 2002. There is no single measure of unemployment for the PRC. Rural unemployment has to be estimated indirectly, urban unemployment figures are based on official registrations for benefits that large numbers of the floating population or those who do not meet the criteria for local registration cannot apply for and do not appear in. Official registered urban unemployment has increased from 3.1% in 2000 to 4.2% in 2004 and stands at approximately 8.3 million (NSBC 2005). Research from the Chinese Academy of Social Sciences (CASS) estimates actual urban unemployment at closer to 10%. Pointedly, unemployment can be of particular vulnerable groups with common cause for dissent—not least the fact that the official system of unemployment fails to recognise their status and provide effective support.

Moreover, the nature of employment can change as the economy grows and this too can be a cause of dissent because new contracts and working practices are themselves sources of dissent. The PRC seems to be developing elements of a classic neoliberal dual track labour market. This is a particular problem for longstanding SOEs that are both under increasing pressure to reduce often hidden losses but also to retain employment and underwrite pre-existing elements of the welfare (especially housing and pensions) and tax systems whilst the new system evolves. From the point of view of the firm flexibility is an opportunity to cut costs by shedding labour or to employ labour in production regimes that exploit them. Since SOE cadres are now managers with a personal profit incentive tensions are often and increasingly resolved in terms of cost cutting. This means that flexibility targets and discriminates



against the most vulnerable elements in the labour force.

Since the state too wants to see SOE costs reduced and to maintain its competitive advantage in labour in other sectors it has little incentive to introduce or effectively implement measures (of which there are already many) that affect costs by enforcing labour rights. The recruitment of business and management into the Party clearly accords with this major tendency within the state and from the point of view of the vulnerable can easily seem to be related, further reducing the legitimacy of the Party. This suggests that the Party is being seen to fail the test of accountability and responsiveness. This failure is to a large degree institutionalised within the social and economic structures of China.

#### *Official Union Organization and Labour Law*

To be legally recognized a union must be a member of the All China Federation of Trade Unions or ACFTU (ICTUR 2005). The ACFTU is subordinate to the CCP (its general secretary is also a member of the Politburo) and operates according to democratic centralist principles. Although the ACFTU participates in the ILO it has not ratified key ILO convention 87 – freedom of association and organization.

Official unionisation in China remains centrally a means of control rather than a means of expression of labour rights. As reform has progressed this has created basic tensions for unionisation that mirror basic tensions within the state and Party concerning the needs of economic growth versus employment. These are expressed in the strictures placed on unions by the 1992 Trade Union Law and its 2001 revision. Article 3 guarantees the right to form a trade union but Article 2 asserts that such unions must be recognized and incorporated by the ACFTU. Article 7 states that the union is required to

motivate workers to meet production clearly indicates this. There is no clear right to strike based on the Trade Union Law, there is no clear and necessary distinction between ownership and union representation (the management can also be the union delegate), and, if a stoppage does occur, Article 27 requires the union to assist the enterprise in resuming production as soon as possible.

Two points emerge. First, the official structure of industrial relations leaves a large proportion of the working population unrepresented (most of the private sector where ACFTU unions are scarce—the ACFTU has 134 million members but China has an “economically active” population of 769 million). Second, the official structure of the system of industrial relations is not set up to effectively reconcile industrial conflict. This is a dangerous situation for the Party and state since reform policy cannot but create industrial relations problems because it is changing the nature of the terms and conditions of employees. The system effectively places dissent outside of the formal institutions, thereby reducing effective conflict resolution and raising the stakes of dissent precisely as reform policy increases the number of workers with grounds for dissent. This is another reason why there were 87,000 recorded protests in 2005 and that the number is increasing year on year. For employees of SOEs the main focus has been redundancy, the collapse of welfare provision, especially the pension guaranteed by the SOE (since if it is restructured the guarantor ceases to exist if its liabilities are not imposed on the new firm), and the failure to pay wages on time.

The Hong Kong based *China Labour Bulletin* and New York based *China Labour Watch* both report that those who organize strikes are often harassed and imprisoned using the criminal law such as “intentional destruction of property” or, more seriously,

are prosecuted for political crimes such as “subversion”, “endangering state safety” and “counter-revolutionary crimes”. The key point is that the internal tension between the basis of reform and growth and the role of the state in representing labour seems to have built into it a tendency for civil society to become more critical (Chen, 2006). The state seems aware of this, as it is also aware of the instabilities created by its failures in the countryside, but again is conflicted in terms of its response.

### *Banking Reform*

One important constraint that is tending to increase the focus on costs to the detriment of labour is the relationship between SOE reform and banking reform based on the failure in the 1990s to resolve the problem of soft-budget constraints.

During reform China has had five main state banks. Under the former system the role of banking was limited, periodically disrupted and primitive—focussing on savings within an economy where money was of limited significance and on the redistribution of capital for investment within the state and collective systems. However, the creation of a private sector, the quasi-privatisation of much of the collective sector (TVEs etc.), the gradual change in status of the SOEs, the growth in the inflow of investment capital into China, and the expansion in personal and private wealth, saving, consumption and expenditure have changed the context within which the banks operate. The banks are increasingly held to international standards of liquidity and solvency and demand the same of clients. This has created a tension in their relationship to the public sector and especially to the SOEs that is accelerating discriminatory effects on labour.

In 1996, Deng’s successor, Jiang Zemin, did announce harsher bankruptcy regulations for the public sector. The policy was termed

“grasp the large release the small” (*zhua da, fang xia*) and was nominally aimed at improving the economic performance of the largest 1,000 SOEs and reducing the financial liability represented by the 150,000 or so others. However, the main focus was on reducing the numbers of enterprises formally designated as SOEs which simply set off a chain of mergers, more leasing and the creation of more joint-stock companies. As such, though the number of SOEs reduced to around 60,000 by 1999 and has continued to fall rapidly thereafter, the problematic relation to taxation and to the banks was not addressed.

State interference has maintained a flow of capital into the SOEs from the banks on the presumption that there should not be any sudden and catastrophic bankruptcies that would cause mass unemployment. However, gradualism does not in itself indicate that effective long-term policies are designed or implemented. In some respects it allows difficult and unpopular decisions with complex causal outcomes to be deferred in a way that actually results in sudden mass unemployment as it has in the case of China. This is not an argument for the plausibility of the Big Leap but it is a retrospective argument for effective, coherent and incremental strategies.

Beginning in 1997 SOEs were allowed to exchange bank debt for shares then held in shell management asset companies whose nominal position was to ensure that SOEs started to earn real profits. Tens of billions of Dollars of debt was converted this way. One plus of this change was that the interest rate burden created by the debt disappeared, allowing losses to be reduced. However, for the system to function share values must be maintained or grow (protecting the banks solvency by balancing or reducing the debt). This creates a motive for the state, the banks and the SOEs to artificially maintain share

value. This in turn creates a motive to over-report revenues and profits for the SOEs reproducing precisely the problem that existed before the exchange with further pressure on the finances of the state and banks that ultimately becomes a pressure for cost cutting within the system.

Between 1997 and the end of 2005 the state expended over \$100 billion in underwriting bad debt at the four main banks. This level of expenditure has created a strong motive to hasten the privatisation and commercialization of the banks. This in turn creates an additional pressure for the state to ensure that the banks meet international liquidity, solvency and practice standards. This is particularly so since commercialising the banks is not just a matter of bringing them into line with international standards but also includes a policy of allowing them to be invested in by foreign banks as part of a commercial flotation process that places them more directly in global financial markets through listing part of their capital valuation.

These changes are a risk for the state banks because the investment exposes them to international scrutiny that further underlies a potential vulnerability in terms of their role as a financial conduit for continued economic growth in China if they feel to attain required standards. This in turn places pressure on the state to resolve the relation between the SOEs and the banks in favour of harsher constraints on the SOEs to enable improvements in liquidity and practices at the banks. For the SOEs this raises the question of restructuring and intensifies the pressure on them begun in 1996 to rationalise their workforce.

### **Working Conditions in China's Private Export Sector**

In 2005, the US imported a total of \$2 trillion in goods and services compared to exports of \$1.3 trillion. Canada was the largest source of imports at \$288 billion followed by China at

\$243 billion (the China figure being a 24% increase on 2004).

According to a recent study by an influential group of economists including Nicholas Lardy, China's cheap exports make the US approximately \$70 billion better off per year by maintaining low cost consumption growth (CSIS 2006). A Republican administration has had little short term incentive to genuinely address an issue that would induce inflation, make shoppers less well-off across the board, and would cause conflicts with major American business that source or have off-shored to China. Furthermore it would require the state to take the position that capital cannot flow to least cost sites in order to expand profits. This would fly in the face of the neo-liberal orthodoxy concerning the growth progressive nature of the dynamics of comparative advantage that underpins arguments for such concepts as positive globalization, the post-industrial society and knowledge economies.

If the US is £70 billion better off because of low cost consumption growth derived from trade with China then by extension China is a low cost source of goods. In terms of the traditional comparative advantage argument the emergence of China reflects lower costs underlying economic specialisation that is mutually beneficial. The presumption is that China also gains because its cost advantage is relative i.e. its populous receive better wages and standards of living than previously as a by-product of new economic activity and this is dynamic as part of economic growth. However, this is not necessarily in a way that is freely chosen by those who actually do the work.

Comparative advantage is a mathematical relation that simply assumes consent. It indicates nothing about the production regimes under which specialisation occurs or the nature of power relations within states and between states. Improvements in information

technology and global infrastructure have facilitated transnational production systems making it more cost effective to develop specific assembly sites for regional and global goods. Moreover, technological change has extended the kinds of goods that can be produced and assembled by a relatively low-skilled workforce. This has meant that low wage costs, longer working hours and higher productivity levels have become prime sources of advantage in the location of both low and hi-tech goods. China, therefore, has been able to extend its range of production and assembly, in a fashion that is historically unusual in its rate, across a wide range of goods.

China's exports increased from \$72 billion in 1991 to \$249 billion in 2000 averaging 13% growth per annum and constituting by 2000 around 25% of GDP. There was then another significant increase in the rate of export growth and its proportion of GDP. Exports reached \$ 593 billion in 2004 constituting around 35% of GDP (NSBC, 2005). According to a recent OECD (2005) report China is now the world's largest exporter of hi-tech and information products including televisions, DVD players, cell phones and computers. China is also the world's largest exporter of shoes, clothing, toys, and textiles. Around 60% of its exports are assembly for re-export from regional and global production systems. Much of this is sub-contracted work in relatively small private enterprises employing from one hundred to a few thousand people and operating on very low margins where the value added in China may be as little as 25%.

The attractiveness of China is precisely these low margins, which in turn rely on production and assembly systems that have been deskilled and in which work patterns can be implemented that maximise productivity and minimise costs. In a deskilled assembly system this effectively means maximising

piece rates and maximising hours i.e. long hours, low wages and few peripheral costs and payments. As such the systems are conducive to exploitative work patterns. Exploitative work relies on a steady stream of powerless labour and China has this in abundance in its migrant labour. Aspects of the new private economy are therefore as prone to discriminatory and socially divisive tendencies as changes that have occurred in the countryside and in the SOEs.

The most dynamic portion of the economy in the last 15 years has been the export sector, and the major growth element within that has been off-shored deskilled assembly. Such work is effectively labour intensive and thus provides a ready source of employment growth to absorb some of the expanding floating population and the increasing numbers being shed from the SOEs. The significance of exports is also reflected in the expanding proportion of GDP taken up by it, indicating the increasing dependency of China's growth on export growth that, in turn, relies on maintaining comparative advantage in a sector that is based on low costs and low margins. As such, there is a ready motive for the state not to implement or enforce rules, regulations and laws that raise costs or affect margins, such as the recent NPC debate concerning rural migrant labour laws and the enforcement of already existing rights. This is a curiously tense situation since the point of encouraging the export sector is precisely to encourage growth that fosters performance regime aims, yet the very basis of the system itself is one that exacerbates division. Those divisions ultimately reside in the structural inequities of global trading systems but they are inequities that the state itself is complicit in. Significantly, however, the state and the Party, so far, have not been the main objects of criticism of the discriminatory effects of economic reform.

Whether China can effectively address the discriminatory nature of some of its production and assembly regimes is centrally a question of whether it can do so and remain an attractive low cost site for sourcing, contracting and location by major global corporations. This is a problem of balance because exports remain a key component in economic growth and employment growth that underpin China's tenuous stability as a performance regime.

One reason for the relative success of China's economy over the reform period is that it did not follow an orthodox economic development model. One might also argue that its use of economic levers to control such things as inflation within the macro-economy has also been non-orthodox since China has tended towards Keynesian approaches. However, its production relations and the shape of its labour markets seem to be increasingly shaped in the image of as well as by a neo-liberal economic order.

## **Conclusion**

Over the last twenty five years determinations on the process of Chinese transition have tended to vacillate from the absurdly optimistic to the apocalyptic. We are currently in an absurdly optimistic phase. Economic journalism in the press is full of statistics concerning record growth levels and the relentless rise of the Chinese Dragon. Western states regularly refer to Chinese growth in fearful tones when talking about the need to liberalise their economies, cut public spending and reduce employment rights and union power. Management and financial consultancies produce impressive projections of returns from investment in China.

A great deal of this is similar in form to the prescriptions that were made in the 1970s that China would not grow. They are simply forecasts of trends in statistical indicators. These are problematic in various ways. They

are only as good as the measures of the indicators and a great deal of the statistics produced in China are problematic (as the bank-SOE relation indicates). In any case, no forecast concerning a society can be accurate over the kind of long term that many are projecting for China at the moment. Claims about the size of China's economy in 2050 are no better than astrology. More importantly, such forecasts are on the basis of the assumption that underlying problems are reconciled by continued policy changes that maintain stability. The point, however, is that they are not analyses of what causes stability and instability and what policies exist to ensure the former. They simply ignore the basic issue that is fundamental to understanding the very thing they want to talk about – what difference China is making and will make. As things stand China is clearly vulnerable to a sudden economic and deep social crisis with global repercussions. Whether this will be the case, however, remains uncertain.

It remains possible that China could manage a rise in its costs reflecting an improvement in its welfare system, its environmental practices and its employment terms and conditions. The very scale of outsourcing to China gives it a degree of leverage in the world economy because there is no obvious single other state into which production and assembly could be substituted. In any case there is the ever-present allure of the size of China's domestic market and the presumption that it will eventually be an economic superpower, both of which tends to make large global firms feel that it makes sense to locate there in order to be within what will be the largest and most powerful economy in the region.

Because China exports more than it imports it has accumulated huge trade surpluses (\$202 billion with the US in 2005) and foreign currency reserves which it in turn

uses to buy Dollar assets such as Treasury Bonds in order to reduce the upward pressure on the Yuan, which in turn both maintains the competitiveness of Chinese exports by keeping the value of the Yuan down and underwrites US federal debt, keeps down US interest rates, and supports the US mortgage bond market, as well as keeping down US inflation through the low cost of imports and debt. As such neither major corporations nor the larger economies such as the US and EU can simply and rapidly disengage from their relations with the Chinese economy without potentially disastrous consequences for themselves. Yet this in itself is a further source of global insecurity and vulnerability because the nature of the asymmetry within dependency can be the subject of political conflict and of expectations led changes in behaviour of key financial actors such as central banks and large hedge funds holding or speculating in the Dollar and Yuan.

These points raise the question of whether a neo-liberal world economic and political order and the actions of individual states within it provide the best solution to issues such as the conditions of labour, environmental degradation, and trade and financial instability. Arguably they do not. Though different states have different attributes and different degrees of leverage and power within the hierarchy of states, no individual state has seemed capable of avoiding negative effects from the system as a whole. China, despite the relative advantages it has enjoyed as a transition economy has increasingly conformed to neo-liberal tenets as it has become increasingly reliant on global trade and export to underpin growth, and this has contributed to the problems identified in section 6 and the tensions within those problems. The US, though hegemonic within the system and able to act in ways that have been to the detriment of other states is also vulnerable precisely because of the

opportunities that the system affords the US – no other state than that with the dominant world currency could have generated such huge budget, trade and current account deficits as America has recently, but in generating them it has become vulnerable to the adverse effects that a rejection of the Dollar or speculation based on the possible rejection of the Dollar would create. The situation of both China and the US indicates that the system within which they are embedded is itself problematic. It is problematic on the basis of the rhetorical notion that a market is “free”, that capital movements should be liberalised to facilitate growth, and that the dynamisms of market-based growth contain the seeds of their own solutions to problems like labour terms and conditions (educate and improve mobility and pay) and to resources and the environment (resolved by price signals as an indicator of viabilities, and by investment and technology). This in turn raises the issue of alternatives that move beyond the small adjustments made by the IMF, World Bank and WTO to their policy positions within neo-liberalism within the past few years.

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## Citizenship

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### **Historical Background**

The concept of citizenship originated in the city-state of Athens, followed by Rome and the cities of medieval Europe. In Athens during the Periclean Age, the city was divided into those who possessed the civil and political rights and participated in the government of the State (Citizens), and those without any rights and unenfranchised (slaves). After the French Revolution, a universal conception of citizenship involving the entire indigenous population emerged (Singh 1958:195).

In Ancient Greece and Rome, a citizen was part of a minority in a City and enjoyed the “freedom” and “special privileges” vested unto him by virtue of his being a Citizen. Slaves, serfs, foreigners and women were excluded from this privilege (Singh 1958:200). In Pericle’s Athens, all vital domestic and foreign matters were referred to debate and decision-making in the citizen’s assembly. (Villa 2001:7). Civic involvement, “a public realm of equality and freedom” along with a ““private” realm where the appreciation of beauty and intellect open[ed] up the possibility of individual self-fashioning” constituted the core of citizenship and statecraft in Athens (p.9-10).

In modern times, citizenship is of two kinds, Natural and Naturalized or Adopted. Natural citizenship is given on the basis of birth or *Jus Soli* or on the basis of descent or *Jus Sanguinis*. Naturalized citizenship is granted through “direct grant or conferment” or through “indirect grant or recognition”. (Singh 1958:197-199) Thus the concept of citizenship essentially involved creation of a legal-juridical and political persona that had special rights as members of the society vested unto him/her as distinct from a non-

member who was denied those rights by politico-legal dis-entitlement. Hence a legal-juridical act of society created a political distinction between two human beings. The essential distinction linked to who may be conferred the right to rule and who may not.

### **Philosophical Underpinnings**

Socrates gave a “dissident, philosophical (notion) of citizenship” based on “moral individualism” and made “avoidance of injustice” as the moral core of the self. Thus “moral individualism and intellectual sobriety became *the* critical standards of justice and civil obligations” thereby leading to “a conscientious, moderately alienated citizenship” (Villa 2001:1-2). Rousseau laid down the foundation of republican form of citizenship when in his *Social Contract* he stated: “Each of us puts his person and his full power in common under the supreme direction of the general will; and in a body we receive each member as an indivisible part of the whole” (Gourevitch 1997:50).

Thus a public person emerged instead of private person as a result of the contract. Associates of such a contract became *people* collectively and *Citizen* individually. In their latter capacity they were “participants in the sovereign authority”. As a Citizen, a man had a general will whereas as an individual he had a particular will that could be distinct from or opposed to the general will or common interest (p.51-52). A Citizen was expected to render all useful services to the State. It was debarred from imposing any unnecessary shackles on him (p.61). Under the social pact, all Citizens were equal. They were to “commit themselves under the same conditions ... enjoy the same rights”. Thus the Sovereign was expected to favor or obligate all Citizens equally and deal with the “body of nation” as such and not with any particular individual. The “respective rights of Sovereign and Citizens extend[ed as far as]



... the Citizens (could) commit themselves to one another, each to all, and all to each” (p.63). Citizens, unlike Subjects, valued individual freedom, security of persons, mild government, prevention of crime and means of subsistence for all. (Ibid.:105) Rousseau seemed to be against the concept of cosmopolitan citizenship. He contended that “those supposed Cosmopolites” justified “their love of fatherland by their love of mankind, boast of loving everyone so that they may have the right to love no one” (p.158).

Pointing out the importance of the acceptability of the Constitution and the laws and their being “good and solid”, he contended that these must rule “the citizen's hearts” otherwise they will be “evaded” (p.179). Thus he provided a radical exposition of the conception of citizenship in a nation as distinct from an idea of a global citizen. He argued for a democratic and legal-juridical conception of citizenship in a nation within the confines of political-geographical boundaries that was consistent with moderate form of liberal nationalism.

Immanuel Kant talked of an “original contract” whereby people accepted to live within the purview of public laws that provide the basis for moral laws that guarantee their basic rights, dignity and autonomy. People, in such a conception, united under a general or common will for reasons of “practical relations with one another”. Kant believed in the eventual appearance of “a cosmopolitan Right” since people had to interact within the given geographical confines of the surface of the earth and the resultant “spatial proximity”. Kant, hence, conceived the idea of global citizenship and foresaw globalization on an extensive scale. His conception of citizenship was more voluntary and associative. It transcended nationalism as well as a political arrangement with the dominance of state and society over individual. Hegel did not

consider the ties between people as being contractual. These were rather “ethical ties”.

He did not seem to accept the eventuality of “a single, liberal cosmopolitan community”. Thus the “ethical life” of one “body politic” differed from the other in as much as the members of one modern state, that is its citizens, shared an “ethical substance” which included “practices, institutions, customs, laws, and a collective memory” as well. All this sculpted “a common political identity”. Since birth, people were “suckled at the breast of universal ethical life”. They passed through an unquestionable socialization process, *Bildung*. This is “a culture that shapes and educates, through which we develop and mature”. *Bildung* was etymologically connected to *Bild* or “picture” in Hegelian conception that expressed the ethical life and spirit of a nation and its citizens.

Citizens then constituted the ethical substance that defined the ethical life (*Sittlichkeit*) of a nation. Common political identity of citizens had a basis in “a natural tie” or identification with “the special character” of a geographical place. Thus according to Hegel, there was a connection between people (*Volk*) and “the natural or geographical features of a land”. It was this “immediate natural determination” that resulted in the difference in the “spirits” of different people. Other bases include “shared accomplishments, memories, possessions, practices, and institutions”. Thus Hegel laid down the basis of an idea of citizenship consistent with the classical form of nationalism and nation-state.

In a multinational state, according to Hegel, “amalgamation” over a long period of time may result in the unification of a modern nation-state and its citizens, thus overcoming the divisiveness of socio-cultural distinctions. Thus the “universal rationality” as embedded in the concept of citizen superseded cultural

particularity with those practicing latter becoming a part of “a rational ethical life incorporating other peoples”. He accepted multi-nationalism, multi-culturalism, multiplicity of religions and multi-linguism amongst the citizens of the same nation-state coexisting with the “universal rationality” and sharing a “spirit”. These members of “a body politic” did not even need to share “manners and education”. An understanding of the identity with fellow citizens generated a “(consciousness) of the whole”. Despite the diversities, citizens must share some basic values. Shared memories and traditions are important to Hegel’s notion of citizenship.

The most significant element in the Hegelian conception is the idea that it is certain practices and institutions, such as private property, contracts, marriages and military service, that bond and unite citizens in a modern state and make them “free” as “meaningful contributors to a shared ethical life”. Discrete and rule-bound practices provided “a coherent set of principles and values, a moral background, shared by its participants”. These gave binding ties, a shared identity and established common interests. Practices and institutions provided “a shared disposition (*Gesinnung*) that (bound) members of an ethical substance” and produced a moral community. Family and civil society ties imparted the “training for citizenship” so as to be a “good citizen”. He stood opposed to “cosmopolitanism as an ideal” in as much as a State merged its independent identity with that of the other and undermines the totality of and autonomy of the self-awareness of its people (*Volk*) (Tunick 2001:69). Hegel gave primacy to nation based citizenship over a conception of global citizenship.

### **Liberal, Libertarian, Republican and Nationalist Conceptions**

Citizenship in the modern sense is the common minimum denominator that allows for an often symbiotic coexistence of diverse and often disparate individual and group identities. Thus it is a means to ensure harmonious political coexistence of fragmented and possibly conflicting identities. A common identity of a citizen is to be sculpted and legally guaranteed to ensure cohabitation of the inheritance of innumerable identities often making contradictory claims on the society. It is seen as “a unifying force in a divided world” (Miller 2000:41). However, attempts to enforce the rationality for such a common identity had often resulted in undermining the diversities present in a society. T. H. Marshall considered *political rights* in a representative democracy, *social rights* such as the rights to welfare with individuals as consumers and *civil rights* with individual as actor, rather than a consumer, with right to freedom of thought, speech, religion, assembly and association, to own property, enter into agreements, right to justice, rule of law ensuring political and social pluralism, as the basis of citizenship (Marshall 1981:141-142).

Whatever type of political system and rights exists, as Raymond Aron points out, “requires from its citizens a certain number of attitudes which define it and give it life”. The representative institutions provide a forum for dialogue between numerous classes, groups, parties, individuals and so on. Citizenship, although providing a common basis, cannot in near future become the basis of “a unified and homogeneous society” (Aron:191-193). It is not only viewed as a legal and political concept but has also been seen to comprise of “ethical element”. It is also understood variously as a liberal concept as well as “a more communitarian understanding of citizenship as entailing responsibilities to promote the common good through active participation in the community life”.

Liberal conception of citizenship incorporates equal civil, political and social rights enjoyed by every member of the society. Each citizen has rights to “entitlements” in the spirit of social and redistributive justice of benefits like free education, health care, housing and other welfare measures that they might not be able to afford. Marshall, the main proponent of this conception defined “(citizenship as requiring) a bond of a different kind, a direct sense of community membership based on loyalty to a civilization which is a common possession”.

Common civilization and heritage entailed entitlements like income, housing, education, health facilities and so on to each member or the citizen constituting the civilization. However, in the current context, the commonality of all civilizations are better comprehended as fractured by manifest and “radical cultural pluralism”. Thus the reference point itself by which the common basis or the citizenship is sought to be defined, that is on the basis of common civilization and heritage or ‘way of life’ becomes a questionable foundation for a liberal conception of citizenship given the plurality that is manifested in the socio-cultural sphere. David Miller sees the very conception of social justice that constitutes the basis of liberal version of citizenship as becoming untenable.

John Rawls seeks to develop a new conception of citizenship based on the premise that “the diversity of comprehensive religious, philosophical and moral doctrines found in modern democratic societies is not a mere historical condition that may soon pass away; it is a permanent feature of the political culture of democracy”. The Rawlsian idea is that a political conception of justice will provide the basis for a citizen to adjudge the “just” nature of political institutions. Political justice will constitute the basis of citizenship

irrespective of plurality of social or cultural positions held by the members of any society. Thus an individual in a liberal democratic society will have a “dual identity”. There will be a personal or private realm, value-system associated with it alongwith voluntary associations or groups to articulate them, on the one hand. On the other, an individual as citizen will agree on principles of justice that constitute the basis of the political institutions and arrangements. In Rawlsian conception, citizen based identity took precedence over personal cultural identity with the latter pursued within the boundaries set forth by the commonly agreed principles of justice that constitute the political realm. Thus the idea of commonality of citizenship preceded personal conceptions of good. The governing principles of a political society had to be acceptable to all. Citizen was not seen as an active participant in the politics as one who although not denied this right, primarily gave his or her consent to the principles of justice governing the society. A minimal participation was needed to protect the rights and liberties.

This was counterposed to the ‘civic humanism’ that essentially recognized an active citizen as a political participant in a democratic society. Citizens identity in this conception was an ‘unencumbered identity’ giving them “the right to view their persons as independent from and as not identified with any particular conception of the good, or scheme of private ends.”

However the private or personal identities of people are “encumbered” ones since they are subject to “certain religious, philosophical, and moral convictions” and “enduring attachments and loyalties”. Unencumbered personal identity may characterize many people in liberal societies giving them freedom to choose their “way of life” unlike those with encumbered personal identities tied to religious, ethnic or some

other cultural characteristic. Latter will have to “concede a good deal” to acquire liberal citizenship perspective and give up many conceptions of cultural form on which ones personal identity is based. For Rawls such a society is based on “free public reason” and mutually acceptable institutions and “forms of arguments”.

In an era of cultural pluralism, it is difficult to evolve a universal or near “majority consensus” based “comprehensive doctrine of good life”. Thus in this conception liberal institutions protect personal identities even though “emasculating many groups politically”. This provides “a set of rights and liberties that give each group at least some chance to pursue its own conception of the good life”. In another variant of liberal citizenship, liberalism and its values are seen as “a distinct and morally contestable way of life” and “political claims and demands” have to be consistent with this distinctiveness. People's identities can then legitimately be channelised in a liberal direction, and cultural pluralism and the conceptions of good life based on them are relegated to the realms of private life and out of the political arena of contest. This variant is best characterized as “militant liberalism” that does not accommodate the plurality of conceptions of good life obtaining in a society.

The libertarian conception of citizenship seeks to make the relationship between the individual and the state “explicitly contractual”. Citizenship is needed because of the demand of goods that need “public provision” and therefore the citizen is “a rational consumer of public goods”. In its extreme interpretation, the libertarian notion of citizenship sees State as “a giant enterprise and the citizens as its (voluntary) customers”. Its moderate version recognizes that “the state must have a monopoly in the enforcement of basic personal and property rights, and the citizens are seen as parties to a universal

contract which gives it that authority”. Therefore the “contract” and the “choice” can provide the citizen who is a consumer the “preferred bundle of public goods” with the State responding efficiently to the demands of its “customer”, that is the citizen. Only a “minimum set of rights” and not any agreement “*in principle*” are then needed between the state and the citizens. Such a conception does away with the redistributive nature of citizenship that entitles a citizen to certain entitlements to counter the market inequities. The libertarian conception then seeks to depoliticize citizenship and “convert the public realm into an ersatz version of the market”. However, in doing so it weakens the sense of citizenship and the identity that goes with it by reducing the rights to a bare minimum.

The republican conception of citizenship is one of participant citizenship whereby a citizen participates in the political debate and the decision-making process that shapes a particular society. Thus active participation and identification with the political community is added to the idea of citizenship that means a set of rights. Republicanism “conjures up the image of a small homogeneous society with common traditions, a shared civil religion and so forth”. Republican conception incorporates the idea of “a general will”, that is, the citizens can reach an agreement through debates and discussions “about what ought to be done”. Such an attempt to seek a common general will may however be disadvantageous to certain groups particularly those that are “oppressed”. Republicanism may seek to enforce homogeneity and exclude “all those defined as different and associated with the body, desire or need influences that might veer citizens away from the standpoint of pure reason”. Republicans hope to reach “a substantial degree of consensus on the issues of common concern” via “open discussion”.

Republican conception of citizenship has problems in accommodating “everything that passes under the name of ‘the politics of identity’” since with legitimate group identities it will not be possible to undertake decision-making in an “open debate”.

Republican view can however accommodate recognizing different group identities by providing them “access to decision-making forums”. However, acceptance of particular group demands, irrespective of their significance to a group's identity is not guaranteed. Any acceptance of a demand has to be “linked to principles that are generally accepted among the citizen body such as principles of equal treatment”. Thus no group can insist on “full recognition of its demands”. Any demand, whether based on personal conviction or group identity can be placed in the political forum. Success or failure of a particular demand will depend on its closeness to “the general political ethos of the community.” In a republican conception of citizenship, no one is, however, barred from placing any demand or is expected to “divest themselves of everything that is particular to them before setting foot in the arenas of politics”. There is however a distinction between the public and private, that is, in a person acting as a private person and as a citizen. Through a public deliberation public/private distinction is made tangible whereby certain matters are deemed to be in the private sphere in which the State and the society cannot interfere and citizens can pursue them via voluntary means. Republican conception, however, gives greater credence to the public participation of “the active and virtuous citizen as a model” as against the private realm of a citizen's life. Republican tradition expects popular participation to some extent in political discourse so that a citizen does not feel alienated from the political system, the laws and the policies and do not treat them as impositions as distinct

from “a reasonable agreement to which he or she has been party”. Thus there is a concern with legitimacy.

Republican conception expects its citizen to “try and persuade the others of the rightness of her cause” unlike liberal conception which seeks to disqualify those conceptions of good that do not accord with the political principles enunciated by the liberal conception. Those who do not agree to regulate their personal conduct in accordance to the boundaries defined by the liberal principles are *personae non gratae*. In case of republican conception only those groups that voluntarily exclude themselves from participating in the political affairs get excluded unlike in case of liberal conception of citizenship where groups may be excluded because they do not participate under “the terms and conditions” of the liberal citizenship. In case of liberals the rights are “entrenched” and have a “pre-political justification” whereas republican conception “grounds them in public discussion”. Liberalism makes judiciary the ultimate arbiters of the constitutional rights whereas in case of republicans it is the “citizen body”. In case of liberal conception of justice some groups may have differences and may just adjust to it for pragmatic reasons. Libertarianism fragments the citizenship retaining the minimal core and leaving the rest of the “citizen rights” to the choice of an individual. Republican alternative seeks to achieve a sort of consensus between individuals and social groups through a form of “give and take politics” via political dialogue. (Miller 2000:44-60)

Republican citizenship has four main postulates, first two of which it shares with liberal conception. First one that is common the latter is that of the security of a set of equal rights that allows a citizen to fulfill private role as well as public one. Second, common postulate is that of following a set of

obligations like respecting just laws, paying reasonable taxes, serving on public bodies and so on. The remaining two that are distinctively republican are willingness to defend the rights of other fellow citizens and promoting common community interests, and finally, expressing political commitment to the community via political participation in formal and informal spheres of politics.

For a large number of people, the “status of citizen” constitutes the core identity of existence. The nature of citizen participation has, in recent times, undergone institutional changes from participation in party politics to other non-institutional forms (such as direct actions like demonstrations). Spending time on political and quasi-political tasks, taking the responsibility of promoting the common good by taking a long-term view of the community interests and subordinating personal interests and values for a broader democratic consensus are vital for republican conception of citizenship. Promoting “public virtue” is key to republican tradition alongwith “strong patriotic loyalty.”

Nationalist identities emerged out of given ethnic identities, particularly the dominant ones. National consciousness was channelised by different social groups according to their perspectives. Political class wanted subjects loyal to the State. Nation became the source of political legitimacy and citizenship its political membership. Idea of common citizenship was thus a product of a compromise and interaction between different groups competing for power. Thus “bounded citizenship” started from the city-states of the yore and subsequently spread to the boundaries of the nation-states as they emerged. Miller contends that an easy access to citizenship undermined the fraternal bonds in the community within the nation-states and weakened the cultural solidarity. In his opinion there cannot be a purely political citizenship sans common and shared public

culture. Thus he argued against a cosmopolitan citizenship. It is however contented that since the nation-states are themselves becoming somewhat anachronistic in the contemporary era, therefore the idea of “bounded citizenship” too is losing relevance. A kind of increasing mutual dependence between the States is on the rise in the global sphere and international mobility of capital within the global markets has increased significantly. International economic interdependence has thus considerably grown (Miller 2000:82-90).

Citizenship has been a partial and a segregationist concept not so long ago in societies, for example, practising apartheid. Citizenship in this case was sole preserve of “civilized” and was denied to “uncivilized” subjects. Some “civilized” natives were however welcomed into the folds of citizenship. These albeit constituted miniscule minority. Latter could have some sort of civil rights but absolutely no political rights. A “propertied franchise” was what separated “civilized” from “uncivilized” or “natives”. Denial of rights of citizenship to these “uncivilized” subjects meant unbridled and centralized despotism. Natives or “uncivilized” were denied civil freedoms that were given to citizens in a civil society. Such discrimination was a part of “urban civil power” and the direct rule as distinct from the indirect rule via “rural tribal authority” (Mamdani 1997:16-18). This was very much akin to the ancient city-states that had introduced a discriminatory form of citizenship vis a vis non-citizens.

Often the concept of citizenship or “civicism”, particularly its legal-juridical aspect, has been taken to “extreme legalisticism” thereby making it a conservative idea attempting to manufacture “standardized juridical-legal individuals as members of a social and political order”. An individual then becomes an “automaton” and

is “caught in the vortex of a political system depriving him/her of the spontaneity that ought to characterize a human being”. Homogenization has been a persistent tendency with the idea and implementation of citizenship in modern societies. This then comes into conflict with the heterogeneity and diversity that marks the reality of different societies. A dynamic 'golden mean' of “appropriate civicism” may provide an answer to a conservative and static variant of citizenship. (Srivastava 2002:118-121.)

### **“Citizen-Customer”, “Citizen-Owner” and “Value-Centered” Models of Citizenship:**

In “citizen-customer” model that emerged with the decline of Welfare State and rise of Thatcherism and Reaganomics, the citizen became a customer, consumer, client or a shareholder. The tax-payers were treated by the governments as a business treats its customers under a “customer service contract”. Citizens Charters and empowerment of citizens vis a vis the bureaucracy were a consequence of this conception of citizenship. In “citizen-owner” model presented by Hidayat Laner Schacter, citizens were the owners of the government and played a proactive role in managing its affairs. They put forth “shareholder” demands to the politicians and public administrators and may not actively participate in the matters of government functioning as “disenfranchised owners”. In “value-centered” model, citizens were the “shareholders” and the government is a “trustee” that manages the “enterprise's assets, programmes and services that deliver value to its citizen investor”. Government was then the agent that was entrusted with “the control, authority and responsibility” to beneficially manage the “public trust and commonwealth of the community” in which the citizens were the co-owners and shareholders but not the proprietors. They however participated in the

communal life and its advancement as co-owners and were to be the equal beneficiaries as well. Citizens then had a stake in increasing the worth of the community. (Jain and Khator 1999:5-6.)

### **Citizenship in the Era of Globalization:**

Globalization was seen to bring about twofold impact on the global scenario. One was that of expanding “the sources of authority of citizenship rights and obligations” to across boundaries of nation-states incorporating international organizations, corporations and international agencies. The other saw a commensurate diminishing of the sovereignty of nation-states. The “taken-for-granted citizenship rights” have been threatened causing internal tensions within the boundaries of the nation-states. (Isin 2000:2) Citizenship as had hitherto existed was seen to need societies and States and “the mutual antagonism they generate(d)” with “non-citizen” or “the other”. A pertinent question is whether “global citizenship” precludes an antagonistic “other” (Urry 2000:76).

Miller contended that the genuine idea of citizenship belonged to the realms of national political communities, or was that of “bounded citizenship”. Transnational or global forms of citizenship were not genuinely possible. He emphasized the Rousseau's formulation of “small-is necessary perspective on citizenship”. (Miller 2000:81-82) The empirical argument for transnational citizenship contended that since self-determination constituted the basis of citizenship it should be applicable at levels beyond the national boundaries depending on the issue at stake. With universality of human rights even the moral ground for taking citizenship beyond the boundaries of a nation-state was covered. Thus people became increasingly responsible to those living across one's own borders as well. Thus there ought to be institutions that operationalize the

transnational or cosmopolitan conception of citizenship.

David Held talked of a democratic legal framework that was cosmopolitan in nature. Such a legal framework regulated the interaction between the States and provided basis for an individual citizen to seek protection and legal remedy if his rights were violated by his or her own State. Thus State sovereignty can be curbed by the international laws and international courts of justice. A nation-state then no longer enjoyed unlimited sovereignty within its political boundaries as it did before. The idea of “concentric circles of citizenship” with democratic citizenship being practiced at different levels like regional and so forth depending on the issues via direct or representative democracy was envisaged.

People had been viewed as members of transnational issue-based communities making them citizens within a global civil society. Such members of global civil society were referred to as “citizen pilgrims” by Richard Falk. These “citizen pilgrims” ultimately sought to build a “compassionate global polity” in future. Miller however refuted these arguments supporting cosmopolitan citizenship. In his view, it had nothing to do with the idea of citizenship that was specific to the nation-state and its historical development. Thus a nation-state accepting jurisdiction of international law did not per se transform its citizens into cosmopolitan citizens. Moreover, a citizen could appeal to the judiciary within the nation-state he or she resided for the redressal of grievances if his or her rights were violated. Thus a domestic enforcement of rights served just as well as international enforcement in democratic States. If democratic rights could be protected through constitutional and legal reforms within the boundaries of a nation-state, they were more preferable than creating transnational bodies

for the same. Latter may tend to apply uniformity in cases where it was neither feasible nor desirable. Although international bodies played a valuable role in several cases creation of sound internal system was a better option. Cosmopolitan laws as the basis of a cosmopolitan citizenship were to be treated with healthy skepticism. Thus “a single arena of citizenship” beyond the nation-state that could be sub-national/regional or transnational based on a difficult-to-define “relevant constituency” and “particular issue” was not a feasible proposition given the nature of contemporary political practices. Any hope of transnational citizenship emerging in future was contingent on strengthening and deepening citizenship and civic virtues within the national boundaries and then hoping that they spread to wider constituencies across the national borders. The idea of “citizen pilgrim” too seemed irrelevant to him because citizenship was rooted in a “determinate community” politically in which the citizens were engaged in “relations of reciprocity” (Miller 2000:90-96).

Those arguing for citizenship beyond the territorial boundaries placed it in the context of “global citizen action” in response to “a new contemporary reality in which power relations at local and global levels (were) increasingly intertwined”. Citizenship had transcended the hitherto sacrosanct boundaries of “national entitlements and obligations”. The new conception was to “*(think) locally* about the impacts of global institutions and global forces (and *act) globally* on them.” Since the policies and programs of global institutions were seen to have a significant impact on the local, national and regional levels, there had to be a response - positive as well as negative, to them. Citizens, cutting across national borders, organized themselves to act on those issues that affected them jointly. Transnational civil societies were seen



as forums keeping a check on the supra-State organizations like the multi-nationals that were otherwise immune to regulation by the nation-states. Transnational linkages were seen to strengthen local voices of protests. Citizens could also act globally *“to realize or promote a set of rights offered to them by global treaties or agreements”*. Several effective global citizens campaigns like for example on universal human rights, against slavery and apartheid, against war and for peace had been launched successfully. It was argued that since the citizenship had been defined in relation to a nation-state, therefore it was not possible to have a concept of global citizenship in the absence of a global State system and government. Others insisted that with the existence of universal human rights, documents like Universal Declaration of Human Rights and other international legal instruments, the idea of a global citizen already existed.

Global citizenship was seen as participation in the decision-making process in social, economic, cultural and political spheres across local, national and global fields. In the absence of clear-cut institutions and authority of global government, citizen action made the global citizenship more tangible. Coming together of “civil society actors” or the global citizens across boundaries had yielded definite results on issues of common interests in terms of getting specific policy changes and other results like spreading civic education, enhancing public debates, increasing transparency and accountability, developing social cohesion and so on. Global citizenship actions had shown diversities of approaches and outcomes. A vertical linkage, alongwith horizontal networks and alliances, running through local, national and global levels brought about enhanced communications and coordination at the multiple levels. These introduced a strong element of understanding

about the local realities. Global citizenship action was supported by participatory research, organizational learning and policy analysis inputs. It required social responsibility and application of ethical and consistent internal behavior and practices so as to be credible, legitimate and effective. Civil society was expected to enhance its capacities to be able to participate fully and effectively in the global decision-making processes in the present era of globalization. It was contended that while a century of struggles brought about citizenship oriented democracies at local and national levels, in the Twenty-first century “the globalization of power” sought global citizen action and extension of democracy at a global level (Edwards & Gaventa 2001:275-287).

## **Conclusion**

The concept and practice of citizenship evolved through long historical time. It emerged as a political idea guaranteeing freedom and equality to members of a civil society. Its boundaries extended from the limited minority that enjoyed the rights and freedoms to a universal application to all members of society irrespective of their origin and status. The struggle to make citizenship a universal concept was neither easy nor without intense conflict. It coincided with the struggle of the subjugated for freedom, equality and dignity. Thus citizenship, as is understood in the current context with fundamental rights and obligations of a citizen, and seen as a product of formation of modern nation-state, is actually a culmination of a long, and protracted struggle for individual freedom within society. Citizenship rights were particularly designed to ensure freedom from state coercion. Experience leaves much to be desired in many parts of the world. Conservative interpretations of citizenship had been undermining and violating comprehensive

fundamental and human rights frequently and in many areas. Instead of being an emancipatory, democratic and revolutionary concept, citizenship has often become an instrument of state domination.

More latterly through globalization, the concept of a global citizen, vis-à-vis universal human rights, had gained greater recognition. There have been conflicting views of whether the high ethnics of 'the global citizen' can be effectively put into practice. The concept of democratic citizenship, guaranteeing freedom and equality, was universal in many ways and had evolved globally over thousands of years. It was not a product of any particular geo-political area. It was global and universal. The acceptance of revolutionary as against conservative variants of citizenship by all societies and people may gain more momentum into the future.

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## Civil and Common Law

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### **Introduction**

The civil law system and the common law system are the two great legal systems of the Western World that developed from medieval resources. In general they are respectively associated with the legal systems on the Continent of Europe (and their former colonies including Latin America) which have Civil Law Codes and the English speaking countries of the world (common law).

### **Duplicate Terminology**

The Civil Law tradition is a system of codes, sometime referred to as “civilian” law. It should be distinguished from two terminological similarities. First, in common law systems “civil law” is used, especially in American law for laws that cover private relations. Consequently commercial law, contracts, divorce, torts, family law, and much more is regarded as “civil law.” This kind of law is covered in the Civil law systems too, but is not called civil law. Second, the term “civil law” has been used for laws that are enforced by the civil government in contrast to canon law enforced by ecclesiastical institutions.

### **Civil Law Tradition**

The civil law tradition has its roots in Roman law. Relatively early in Rome’s history the customary law was published in stone as the Twelve Tables (451 B. C.).

The committing of the orally transmitted law of customary practice to writing was done in part to make it publicly known. Writing it as a publicly visible and objective plain law gave greater security to the Plebeians who felt that they were being victimized by the Patricians who were the ones who knew the

orally transmitted customary law. The Plebeians suspected that the unwritten customary law worked too well to the advantage of the Patricians.

The Romans had private law which was called the *ius civile*. This was law that could only be applied between Roman citizens. An idea that existed then as well as at other times is that people carry their law with them.

With the development of the Roman Empire there arose the need for adjudicating cases between the many different peoples who were now subjects of Rome, each with their own law. To meet this need there arose the *ius gentium*. The *ius gentium* was developed by Rome's agents over a number of centuries. Its principles were often derived from reason. The Stoic philosophy of the universal logos that governed the universe gave to each person reason. With reason a universal natural law that was common to all people could be used by Roman judges to judge between the subject peoples the Romans governed. After most of the people of the Roman Empire became citizens the *ius gentium* eventually merged with the *ius civile*.

Between the end of the Roman Republic and the end of the Roman Empire a number of attempts were made to reorganize and update Roman law. The last republication of the law was the work of the Emperor Justinian. He had the Roman law "modernized" and then sought to destroy older versions of the Roman law. Soon thereafter the barbarian invasions eclipsed the Roman law. The customary law of the Goths, Lombards, and other tribes prevailed until the Roman law was rediscovered in the high Middle Ages.

By the time of the Reformation some of the newer schools and universities in France and Italy were teaching the revived Roman Law. It spread to a variety of places on the Continent of Europe, but it was changed or often adopted only in part.

## French Civil Code

In 1804 Emperor Napoleon Bonaparte had the Roman civil law code reworked and published as the French Civil Code (*Code civil des Francais*) which was soon called the *Code Napoleon*, and later the *Code civil*. It was a matter he considered as a lasting legacy.

The *Code civil* issued in 1804 did not cover all topics of the law. It only covered private or interpersonal relations. This included matters such as family law, inheritance, property transactions, simple commerce, contracts, torts, and similar matters.

The *Code* had been finished in 1801 but it was not adopted until March 21, 1804 because it was not considered revolutionary enough. It was published in 1804 as the *Code civil des Francais*, but was rename the *Code Napoleon* in 1807. By abolishing the old order, giving rights to women, and other changes it permanently changed the French economic, legal and social order.

When it was promulgated the *Code* contained a Preliminary Title and three Books. The Preliminary Title how the code would take effect after its promulgation. The Books were subdivided into Titles covering different topics. The Titles were then subdivided into chapter and sections containing laws. The laws covered three main topics—persons, property and actions involving persons and property. This arrangement followed the organization scheme of the Roman Law from the Roman juris, Gaius.

The law of persons was put into Book I. Title I of the Code registered topics of the enjoyment and privation of civil rights by describing how citizenship could be gained or lost. Title II described personal events of interest to the state—births, marriage, and

death. It also described how official records were to be kept.

The third title in Book I treated matters of legal residence. Title IV discussed how the property of someone long absent from the country was to be handled. Title V discussed marriage and Title VI treated divorce and legal separation. Titles VII and VIII contained the laws covering paternity and adoption. The rights and duties of parents and guardians were covered in Titles IX, X, and XI.

The second part, Book II, was organized into four titles. Each of these was concerned with property. Title I defined and covered legal principles concerned with immoveable property. The other three titles treated usufruct and manorial services.

The longest part of the *Code* was Book III. It contained numerous actions that could be taken involving persons and property. Its theme “Of the Different Modes of Acquiring Property” revealed that property was of great concern. In all there were 2,228 articles in the *Code* treating the subject of property.

Book III’s Title I contained four chapters on the numerous ways that property could be transferred upon the death of an owner. Among other things it also covered the ways in which property was to be distributed in the case of the death of a group of people. It also excluded from gain any who might have committed a felonious act(s) with the hope of profiting thereby.

Title II of Book III covered property bequests and wills. It forbade entail and physicians from inheriting the property of their patients. In a similar manner it prohibited the officers of ships from profiting from the will of one of their sailors if the will was made by the deceased sailor while under sail.

The third title of Book II covered the law of contracts. Six chapters were devoted to the subject covering all manner of contractual

issues and problems including the making of oaths in contracts.

Title IV, Book III, dealt with “quasi-contracts.” These were actions included liability for causes caused by someone actions that hurt the property of another. Title V covered at length the “community” created by marriage. This meant that by marriage all of the property of the two individuals became the common property of their community. Only if it had been excluded in writing in the presence of a notary prior to the marriage was it excluded. It also made the husband the head of the legal community. By doing so it limited the rights of the wives to make contracts without the permission of their husbands.

In Title VI of Book III the manner of making contracts for the sale of real estate or consumable good was decreed. Title VII covered barter. Title VIII covered renting and hiring real estate or farms. Labor contracts were covered in Chapter III of Title VIII.

Titles IX-XV covered partnerships, loans, deposits, securities, pledging as a part of security, annuities. Betting was treated as a different activity from insurance.

Title XVI described numerous activities that could justify the issuing of a warrant for arrest. Selling fraudulently property or other forms of malfeasance were clearly described. Title XVIII covered mortgages and evictions.

The Code made the judges responsible for finding the facts in a case and then for applying the code to the facts. To fail to do so would warrant prosecution for the denial of justice.

Other codes followed the Civil Code. The other codes covered civil procedure, commerce, criminal procedures and agriculture. The Penal Code was adopted in 1810.

The *Code civil* was developed by prominent legal scholars. These jurists issued what was in essence a clearly stated legal rule book. The law in general could be read and

understood by most literate people. The Code once developed by the jurists was then examined by the French legislature which then adopted it as law. It was soon joined by other companion codes on agriculture, criminal law and other topics.

### **Ancien Regime Legal Complexity**

There were several factors driving the development of the French Civil Code. The new Code was very rational. It was easily understood for the most part by common sense reasoning. It seemed to be an application of the reason to human relations that was universal and which could easily be adopted everywhere in the world. This thinking was an expression of the love of Reason that inspired many of the thinkers of the Enlightenment and the French Revolution.

Another reason lay in the confusing mosaic of laws that had existed in France prior to the French Revolution. It is almost an exaggeration to call the French legal system of the *Ancien Regime* a system. It was a confusing stew of different types of laws that had grown up over the past thousand or more years. In southern France some parts of the old Roman law shaped the legal relations of people. While in contrast in northern France there was a wide variety of customary laws that formed a different kind of legal tradition.

There were 368 local codes and such complexity that attorneys from one locality could not practice in another because the laws varied so much. Knowledge of the law in one area was useless in another.

Also the Roman Catholic Church was a part of the legal system. It had virtual control of the laws regulating marriage and family. Its ecclesiastical courts tried a variety of cases with its own legal staff that included in the 1600s the father of Rene de Cartes and others.

The system also was layers with ancient monopolies, privileges, vested interests and with aristocratic rights. The status of

aristocratic meant unequal treatment by the law in cases involving aristocrats and common people.

Because the judges in the system of the Ancien Regime were almost always drawn from the aristocratic class they were viewed by the common people as respecters of persons in cases. In short their decisions were calculated to uphold privileges of the aristocracy and which in their view frequently denied them justice.

The French Revolution abolished the feudal system of ancient rights and privileges and moved in the direction of a single system of equal justice. Napoleon having joined the Revolution also adopted its aspirations.

### **Spread of the Civil Code**

During the Napoleonic Wars the French usually imposed the *Code civil* upon the countries they occupied. In some cases the usefulness of the code caused it to remain after the French had departed.

The Civil Code was introduced into areas under French control in 1804. These included some of western Germany, northwestern Italy, Geneva, Belgium, Luxembourg, and Monaco. Other territories subjected to the Code included Italy, the Netherlands, the Hanseatic League lands, and Switzerland. The lasting influence of the Code in these areas was directly dependant upon the length of time in which it was in effect.

In colonies controlled by France the Civil code was willingly adopted, but almost always with modifications. The civil law codes of France which soon influenced the law in Spain spread to their colonies.

Today in Canada the Province of Quebec follows the civil law code. In the United States Louisiana, with its French and Spanish heritage, follows a modified civil code. The Napoleonic Code of Louisiana is not the same as the French code. Rather the law is a mixture of the French code, Roman Law and

other elements. The code in Quebec is also not pure French, but a mixture as in Louisiana.

Puerto Rico and the Virgin Islands follow a civil code derived from Spain as does Hispanic America. Vestiges of the civil law code exist in Texas and California where after marriage all property is considered "community property." Other countries with civil law codes include South Africa with its Dutch Roman law.

The civil law is legislated as a complete code. The judge(s) in cases will then apply the general principles in the code to a particular case. Precedents are not binding, but may be influential as "La Jurisprudence."

### **Common Law**

The common law is the name for the main system of laws and legal practices in England and Wales, most of North America and in other countries that were once part of the British Empire. It is the accumulation of precedents in case decisions, statutes, ruling and even the application of customary law.

The common law developed in England after the Norman Conquest in 1066. England at that time was populated by diverse peoples. Along with Angles, Saxons, Danes and other people there were now Normans. These different peoples had different laws. Most law at the time was customary and of limited development. To unify the country the Norman kings sent out itinerant judges (Justices in Eyre) to travel a circuit. These judges were usually monks trained in canon law, with a smattering of Roman law that was just then being revived. As the judges held court from place to place they would decide cases using the Bible, canon law, and most especially reasoning applied to the customary law of that place. The customary law was usually unwritten, but had been exercised in the various local courts prior to the Conquest.

When the judges returned to London they where they were resident in taverns that eventually became Inns of Court, they would discuss their respective cases. In the course of over two hundred years they "discovered" the law common to all the people of England. In effect they were developing legal principles as they made judicial rulings in particular cases. Among the principles of the common law are *stare decisis* (Latin for "let the decision stand."). *Stare decisis* means that a judge in deciding a case will consider other similar cases (like cases should be tried alike) and if there is a similar case that has established a precedent then the precedent will be the rule that will be applied. However, in the absence of a rule (or a statute in modern times) the judge will in effect "legislate" and create a new rule. This means that common law is case law or judge made law created by legal reasoning about a legal problem.

The development of the common law is similar to the process of building of a coral reef. The slow accretion of decisions, laid down case-by-case, allows a body of common law to develop. The decisions in numerous similar cases allow little distinctions to accumulate until a new situation arises. The new conditions are then ripe for a new rule of law.

The practice of following precedents which are binding upon lower courts or upon future similar decisions within a particular judicatory, gives stability to law. However, if a decision in a case is similar to a case currently under consideration the judge may accept it as only a persuasive or compelling decision if it come for outside of the judge's legal system. For example in the United States precedent in any state will be only persuasive for all other states, while the decisions of higher courts within that state will be binding.

The slow grow of the common law in earlier centuries met the needs of the times.

However, law needs to have both stability and flexibility to meet changing needs, or to meet inadequacies in the law. Since the common law was rigid and inflexible, and because to bring a case to court in the common law courts was difficult and expensive for the majority of people in England at that time, a remedy was provided. The king as God's vice-regent on earth was the fountainhead of justice in the law, so appeals to the "king's conscience" for justice led to the development of Chancery courts where the law was based on abstract moral principles. This kind of law is called equity law. In time there were periods of conflict between the common law courts and the equity courts. For many centuries there were several types of courts in England that could give conflicting rulings. This tension moved to American when the American colonies received the common law. It is to be found in the Constitution of the United States (Article III, Section 2) where the judicial power "shall extend to all cases, in law (common) and equity..."

Today most states and the government of the United States have abolished separate equity courts. However, the law still exists. Equity law has merged with common law. More precisely a judge has to decide if a case is a common law case or an equity case. Frequently this cannot be done apart from trying the case.

At the time of the American Revolution common law prevailed in all the colonies. It was viewed as a bulwark against the claims of the Crown which view the colonies as fiefs ineligible to the protections of the "rights of Englishmen."

Following the Revolution there was opposition to keeping the common law in some quarters; however, it was not strong enough to supplant the influence of the common law jurists, like William Blackstone, or Edward Coke, whose writings had been a part of the "reading of the law" of Colonial

American lawyers. Some states did adopt laws forbidding the citation of English common law cases; however, the practice did not last long. The practice in most states is like that in California where the English common law is cited as an ultimate resource.

It is now common for cases to be cited from among the several common law countries. An English case may cite an American or Australian case just as easily as the others may cite an English case. The development of the internet and the digitizing of the vast literature of appellate cases are making finding the law easier.

Civil law jurists had a small impact on the development of American law in the early decades of the Republic. Virtually all of these were French civilians, but the adoption of civil law was never widely contemplated.

The common law is the legal backdrop of forty-nine of the American states. Most cases tried in the United States are state cases. Most of these are matters of private law (civil) rather than public law. The federal government's courts on the other hand usually are interpreters of statutes or of the Constitution. In this role they have on numerous occasions used principles and usages of the common law as part of their legal reasoning. State judges also do the same.

Strictly speaking there is no federal common law. United States Supreme Court Justice Joseph Story was an advocate of federal common law. It dominates his decision in *Swift v. Tyson*, 41 U. S. 1 (1842). However, Justice Louis D. Brandeis in *Erie Railroad Company v. Tompkins*, 304 U. S. 64 (1938) effectively eliminated this idea. The crux of the problem is that the Constitution (Article VI. Paragraph 2) made federal law supreme. A federal common law would therefore be the supreme law of the law and effectively nationalize the common law.

In modern times attempts have been made to replace common law with statutes. Even in areas where common law has been dominant such as commercial law, contracts, and torts efforts have been made to create uniform codes. Even here the common law still gains new life. Uniform codes are often preferred by big business or by those doing business across numerous state boundaries. The desire for uniformity has given rise to pressures to adopt statutes which will function like a civil code. However, the dual court system of the United States with its fifty state courts systems, the federal judiciary, and the dependencies such as the Commonwealth of Puerto Rico, allows for cases arising in these many jurisdictions to be decided by courts that may create conflicting interpretations of the same uniform code. These then become locally binding precedents.

In addition it should be noted that an endless stream of new issues come before the courts on an almost daily basis. An example is the case of *Davis v Davis v King and Seven Frozen Embryos*, 842 S.W.2d 588, 597 (Tenn. 1992). The case involved seven frozen embryos as the object of dispute between Junior L. Davis and his ex-wife Mary Sue Davis. The science of in vitro fertilization was new and this was an original unprecedented case.

The fertility clinic was also brought into the fray as a third party. The issue was whether the ex-wife, who had suffered five tubal pregnancies, could use the embryos in an effort to become pregnant. The ex-husband was opposed.

The judge narrowed the legal issue to the disposition of the seven cryogenically frozen embryos maintained by the fertility clinic. The case arising from the development of a late Twentieth Century advance in fertility medicine was without precedent. The decision of the Court was not a substitution of the Court's theory of public policy for that of the



Tennessee legislature. In the absence of any statute the decision was a further development of the common law. The Court was compelled to render justice in the case, pronouncing the law as it was found in the case.

The judge went to great lengths in the light of the controversy surrounding the case to precisely state the reasons for the decision. The emphasis was upon the finding of fact and the reasoning that was made from them. The decision thereby became a modern example of the tradition of the common law made by judges for the last thousand years.

### **Criminal Law**

Criminal law is public law. While private law deals with the relationships between private persons or with the government in private actions, criminal law punishes offenders of the public peace. Most of the criminal offenses prosecuted in the United States today differ little from the types of crimes prosecuted in the English Middle Ages.

In a criminal case the paramount issue is "what happened?" It is in the criminal law that significant differences between the civil law code and the common law can be seen. To establish the facts in the case in the civil law the proceeding are inquisitorial and held before a tribunal where a judge(s) hears the case. This means that the government's prosecutor and even the judge in a criminal case are seeking to establish the facts. The judge can even intervene to probe witnesses for either the prosecution or the defense, especially if the judge believes that the defense or prosecution is not being aggressive enough.

In a common law system the proceedings are adversarial in both actions in private law cases ("civil actions") and in criminal cases. The courtroom scene is a ritualized "trial by combat." Two knights fighting as champions of the accused or of the accuser was a practice from the Norman knights who invaded

England. The loss by the champion of the accused could mean death for the accused. The belief that God was on the side of right always, supported this practice. However, in the modern court room the champions are attorneys, the weapons are legal motions, oral arguments, and physical evidence. The results can be just as devastating for a defendant whose attorney loses as being burned as the stake was in the Middle Ages.

The judge in the common law courtroom is a neutral umpire who regulates the combat of the attorneys. The jury is the "trier of fact." The jury is an institution that has withstood a number of attempts to find fault with it through modern scientific methods of research. The grand jury composed of twenty-three persons decides that a crime has been committed and then with the evidence pointing to someone(s) orders the accused to stand trial to answer the charges in the indictment or true bill. The petit jury (little jury) then tries the case.

In civil law tradition the judge in an appellate case can reverse the facts or reinvestigate the facts. However, in the common law system, as least in the United States, the jury establishes the facts. These cannot be retried by an appellate court. Appeals seek the retrial the law applied in the cases that arise from trial courts.

Another difference between common and civil law systems is that the judges in civil law tradition are trained as judges in university law schools. They may or may not practice as attorneys. In contrast judges in the common law system are mostly recruited from practicing attorneys. (There are still a few places where a layman will try minor offenses or cases.) Common law judges may receive some training after election or appointment as a judge, but they have none prior to being made a judge.

## Present and Future Developments

Civil law has spread to China and beyond since 1945. It is growing rapidly in Europe with the growth of the European Union. What began in 1951 as an agreement on coal and steel has grown into a legislative unity organized into a code. However, even in the civil law traditions the number of new situations that arise in the rapid social, economic and political changes caused by the dynamics of modern technology can outstrip the capacity for static codes to meet new situation as effectively as the common law. This means that there are times when the tribunals act like common law judges. The presence of English judges on the European Court of Justice and the European Court of Human Rights is also having an impact.

English participation in the European Union is having a modifying effect on the original home of the common law. How this will eventually affect the English is too early to tell, has been demonstrated in a number of cases involving the rights of the accused or the rights of those who might be deported because of sympathies or participation in radical Islamic movements including the threat of acts of terrorism.

There are also areas of law such as international law in commerce that are lacking in statutes because there is no legislature with the authority to make enactments. Consequently a kind of international common law exists in a number of areas of international law. The attempts of European Union countries to establish international courts of justice claiming sovereignty over sovereign nation-states so that the crimes of dictators are punished is an attempt to enforce a civil law tradition code where there has never been law.

In the United States and other common law countries the complexity of modern society, especially where agencies are created to be regulatory bodies has restricted

somewhat the opportunity for common law jurists to exercise their talents. When important cases go to arbitration the opportunity for common law to develop on an international basis is increased.

The civil and common law systems are both a thousand years old. Both have influenced much of the world far beyond their points of origin. As the Twenty-First Century advances it is reasonable to expect that the many social, economic and political changes driving the transformation of the world will give opportunities for both of these systems to develop new ways to regulate human relations in the quest for justice.

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### **Introduction**

Constitutional political economy began as a discipline that applies economic analysis to the choice of rules, and thus of institutions, going so far as to formalize them in legal terms. Taking this approach, constitutions are considered not as exogenously given, but as the product of negotiations between the agents involved.

We can assume that constitutional economics can be split into two branches, i.e. positive and normative. In *positive* constitutional economics, we analyze the way in which constitutions are formed, i.e. the institutionalized and regulated social rules, and the methods used to change them. *Normative* constitutional economics, being linked to the political theory of constitutionalism, focuses on the processes that generate constitutions consistent with the principles of constitutionalism.

The research program of constitutional economics stems from the realization that the choices between rules, or institutions, cannot be analyzed to satisfaction using the neoclassical approach, and particularly the neoclassical theory of welfare, according to which politicians are well-intentioned agents, or at worst they may be indifferent to the maximization of their own individual utility functions. There is no such assumption in the works of the theorists of constitutional economics, who instead see politicians as agents with their own utility functions, which are not necessarily consistent with those of their electorate (the principals).

Another open question in constitutional economics concerns the relationship between social results and the criteria adopted in making choices. While the neoclassical approach to the welfare economics sees no

relationship between the said two topics, for constitutional economics such a relationship must necessarily exist.

### **Institutions**

Assuming that people, be they political or economic agents, take actions in a context marked by uncertainty, asymmetry of information and variability of behavior, these agents will naturally find it useful to establish stable and socially accepted rules of behavior, that we can call "institutions". Going along with Schotter (1981, p.109), we can say that institutions are the outcome of the rational behavior of agents with incomplete information available. Social and economic institutions are therefore tools for increasing the informative content of political or economic events, or when prices alone are not enough to throw light on the situation (*ibidem*). So an institution's ability to function depends on its rationality, i.e. on its capacity for reducing the relational uncertainty between the members of a group (North 1998).

Institutions are thus required to assure stability of the forms of social organization, as the functionalist approach in anthropology always used to emphasize. An important issue in the context of economic research on a topic of institutions lies in the emergence of these institutions, their progressive formation according to a logic which is necessarily evolutionary. The way in which institutions develop as a result of actions prompted by the perception of individual interest has been amply studied using game theory (Axelrod, 1984; Nurmi, 1998; Aoki, 2001), where social norms are seen essentially as conventions, i.e. as behavioral conformities not necessarily based on an explicit agreement between the agents, that stem from their individual interests. Here again, social norms are acknowledged a sort of "implicit function" with a view to improving the

amount of coordination between the parties, without necessarily serving any particular project, as envisaged by Buchanan and Tullock (1962).

Game theory clearly takes considerable interest in the processes behind the formation of shared social rules. Of course, it should also be said that an important part of the contributions on the matter of game theory concerns both competitive games and weakly cooperative games, i.e. games giving rise to implicitly cooperative institutions, that are determined spontaneously as the games develop. To some degree, they are games that take their cue from the prisoner's dilemma to demonstrate how situations where a mutual distrust prevails between the agents will give rise to behavioral rules that offer lower payoffs than the payoffs that could be achieved by adopting a behavior inspired by loyalty and trust.

As for the individuals playing the game, the outcome of opportunist behavior is presumably determined rationally when these agents have the opportunity to interact over a lengthy, theoretically infinite period of time. If the agents are rational, they can establish institutions inspired by a cooperative logic and thereby create rules for sharing their surplus, thus introducing a general principle according to which they are able to choose between different rules of behavior. Such choices may be made spontaneously, or they may be due to a public decision process.

One of the founding fathers of constitutional economics, Buchanan, defines the constitution as, "a set of rules which constrain the activities of persons and agents in the pursuits of their own ends and objectives" (1990:3). Buchanan basically says that no single individual's objectives or universe of values are in themselves superior to those of anyone else (Voigt 1999:9). As a result, everyone is entitled to pursue their own goals providing they do so in compliance with

certain fundamental rules. Of course, these rules must be shared and Buchanan derives a procedural criterion for identifying which rules the agents can share. This criterion is based on Knut Wicksell's idea (1896) that agreements for the private exchange of goods are advantageous inasmuch as the agents involved are voluntarily party to them. An agreement is considered advantageous if all the parties expect to obtain a greater payoff with the agreement than without it.

As we said earlier, the existence of a potential advantage does not necessarily give rise to an agreement. Doubts about being party to an agreement stem from the risk of the other party manifesting an opportunist behavior. In this light, it becomes useful - not to say essential - to create a legal commitment guaranteed by an outside authority. Buchanan himself (1990) said that a fundamental difference between standard economics and constitutional economics lies in that, while in standard economics agents make choices within a given set of constraints, in constitutional economics agents choose between constraints, in the sense that their first concern is how to define the rules of the game.

In standard economics, therefore, agents choose the most suitable action in the light of existing constitutional constraints. The fundamental constraint considered by orthodox economics is the availability of endowments. Given this constraint, subjects choose the course of action that maximizes their utility function. In constitutional economics, on the other hand, agents choose the most suitable constraints for solving the problem of how best to express possible interactions between the agents. The main topic of constitutional economics concerns using the methods of economic science to analyze the processes that shape political-institutional rules.

## Principles for Establishing Rules

If there are more than one agent involved and the agents constitute a "society", we can assume that a rule is advantageous providing every member has spontaneously approved it, which means that the rule is established using a criterion of unanimity. The fact that a rule has been adopted unanimously does not cancel the risk of some members of the society developing an opportunist behavior, however, so it may be necessary to appoint someone as a referee to judge a situation and, where necessary, apply sanctions. An institution is thus converted into a constitution. The role of constituent judge may be assigned to the state or delegated to other bodies. Clearly, the aim of the constituent judge may be to ensure that there is no opportunist behavior, or it may be to guarantee, by means of a specific decision process, that members of the community can gain access to public goods that would be inaccessible to them individually.

A suitable decision process is derived for the said purpose when the social rules adopted are not always shared by all the members of the society, so a rule cannot always be derived from the unanimous vote of the agents. In point of fact, if the concept of unanimity were strictly applied, it would be materially impossible to establish rules to ensure that a surplus is produced both in the aggregate payoff and in the individual payoffs. Very often the rule of unanimity has to be abandoned and this happens, as we have said, when decisions have to be made on the matter of the production of public goods.

If the problem remains how we arrive at the procedures for establishing the rules, there are two fundamental ways in which we can imagine the evolutionary construction of a system of rules. One of these lies in Buchanan's theory, which assumes that the rules are constructed by agents with an Olympian rationality and consequently

capable of identifying the most suitable rules for serving their purpose. The other lies in the approach taken by Hayek (1979), which assumes the existence of societies with predefined rules that its members do not necessarily understand. The subsequent interaction between the environment and a society can give rise to new rules, which are adopted by the society's members to coordinate their behavior. To a large degree, this coordination of their actions takes place spontaneously, but it is not unusual to find situations in which an outside power is needed, i.e. a government capable of imposing compliance with certain rules of conduct. We can see here that Hayek's approach is evolutionary in the sense that the groups which coordinate their actions with the rules prove more efficient than those which fail to do so, and former eventually prevail. In a sense, there is a Darwinian selection of the rules. Implicit in this interpretation, there remains the issue of how more efficient rules are established, especially if the definition of efficiency is accompanied by a value being attributed to the nature of said rules.

Conversely, Buchanan's approach emphasizes that the constitution is a contract between the members of a society, a sort of social pact. The concept of contract presupposes an exchange between the society's members, however, which means the opportunity to transfer ownership rights. But if the constitution is seen as a sort of meta-contract, it is hard to imagine it being based on a set of ownership rights, since the main purpose of a constitution is to establish these rights at the outset. Probably, if we combine Hayek's and Buchanan's approaches, we may be able to find the path that leads to the establishment of constitutional rules; the members of a society may well "construct" new rules with the materials of which the old rules were made, but combining these

materials in different proportions, as it were, to derive "new" rules (Mistri 2003).

In a sense, this way of looking at economic constitutions comes closer to the view taken by Hardin (1989), who describes a constitution as a set of conventions according to the approach of game theory. Taking this view, constitutions are tools for better coordinating the actions of different agents, working on the assumption that none of the agents would be capable of improving their position by departing from the rules formulated in this way (Voigt 2003:XII).

### **Institutions and Bounded Rationality**

In any case, an important problem, if not *the* problem in the theory of constitutional economics, consists in how a new constitution takes shape. In entirely general terms, the emergence of a new constitution can be seen as a sort of adaptation by the system of constitutions to changes in the outside environment. The adaptation processes may take quite a long time, so the "new" constitutions emerge after a suitable period of gestation. Dynamically the picture is one of "punctuated equilibria", but genetically the constitutions are the outcome of logical couplings between environmental change, social dynamics and cognitive processes.

The role of the cognitive processes seems significant because constitutions are seen as tools for solving coordination problems. This means that agents must have an adequate understanding of the nature and the logical structure of the problem they need to solve, and they must be capable of evaluating the consistency between the aims and the results of the process for constructing a new constitution. It is hardly surprising that Buchanan and Tullock (1962) should have emphasized the ability of an economic constitution to bypass the cognitive constraints that increase the agents' computational uncertainty. The assumption

that the agents' rationality is bounded affects the methods used by the agents to construct their strategies, and these methods belong to the world of *procedural* rationality.

In fact, from the point of view of constitutional economics, the subjects' rationality will be defined on the basis of the decision-making procedures they use, rather than on the substance of their decisions as in the case of standard economics. We can thus say that the constitutional rules that governments adopt to solve coordination problems can be seen as functions of the procedures they use, and they are necessarily affected by said procedures. The choice of the procedures is therefore not without influence in the determination of the constitutional rules, since different procedures can lead to different rules.

The shaping and adoption of social rules can thus be seen as the outcome of a sort of learning process defined on an open set of potential rules that the members of a group create rather than choose (Vanberg, 1994, p.29). This can only come about if we assume that there is a group, however it may be defined and whatever its composition. The group may form around a new problem, but as a rule it already exists and the rules that it develops are influenced by the heritage of rules that the group already used beforehand. Some of these rules have the nature of political constitutions, i.e. of norms that have been codified using the tools of politics.

Having come thus far, we need to answer a fundamental question posed by Buchanan and Tullock (1962:V), who wonder whether there is a rational economic explanation for the formation of political institutions. The question is legitimate in that we are bound to wonder how the individualist assumptions of political economy can be compatible with the adoption of a political constitution. So we must ask ourselves why free and rational individuals choose to maximize their utility

by means of a collectively organized action rather than by individually pursuing their goal. The answer that Buchanan and Tullock give is that individuals will decide to consider organizing a given activity politically when they expect to achieve a greater utility from doing so.

There are fundamentally two criteria that individuals may adopt. First of all, a political (or collectively organized) action may eliminate some of the *external costs* that a private action by other individuals might bring to bear on the individual in question. Secondly, the collectively organized action may prove necessary in order to achieve *external benefits* that could not be achieved by means of a private action - take, for instance, the creation of an army to defend the frontiers, and the group, against attack from outside. For the purposes of assessing the various organizational options, Buchanan and Tullock suggest adopting a "cost"-based approach and considering the political action as a means for reducing the external costs that individuals would have to pay for purely private or voluntary actions.

The utility that individuals derive from any human activity is thus maximized when each individual's share of the "net costs" of their participation in this activity is minimized. The costs we are talking about are essentially the *costs of interdependence*, and the identification of new constitutional forms stems from attempts to reduce the costs of interdependence. According to Buchanan and Tullock, analyzing these costs enables us to decide which activities to assign to the private or public sectors. Individuals must therefore consider the possibility of collectively organizing all the activities that would presumably carry higher costs of interdependence if they were organized privately. Individuals will opt for one or other alternative on the strength of a comparison of the expected costs of interdependence and the

expected costs deriving from the creation of a specific political organization.

An individual's choice must be compared, however, with choice made by the other individuals, and this gives rise to costs deriving from the choice of decision-making method. It goes without saying that no decision-making method is neutral in relation to the achievement of the goals that each individual is aiming for, so a rational individual must have different decision-making methods to choose from. To a large extent, the various options are subject to the political system in force, so we can choose rules inspired by the criterion of unanimity or rules inspired by some majority vote criterion.

The criterion of unanimity is designed to safeguard the rights or interests of each individual. Of course, this may mean that - in the event of it proving impossible to arrive at a unanimous vote - the final decision is to maintain the status quo. The majority vote criterion, on the other hand, is designed to safeguard the interests and rights of the majority of the group's members. In practice, this is easy to do when there is only one topic under discussion, but - based on Arrow's "theorem of impossibility" (1951) - it is highly unlikely that consistent majorities will emerge for each topic when there are more than one. "Expedients" can be used, however, to evade deadlocks, unless we want to go for a rigidly totalitarian system.

### **Example I – Creation of the Euro**

The birth of the European common currency (Euro) after the Maastricht Treaty is a useful example of what it means to switch from one constitution (a monetary one in this case) to another. The European countries had already adopted guidelines on how to deal with the coordination problems deriving from the goal of economic integration, of which monetary integration was a part. Although monetary integration was one of the



objectives in the various agreements reached by the European countries, it seemed harder to achieve because that it was impossible to reconcile the goal of economic growth with that stable exchange rates. It is also worth noting that the agents involved in this case were not single individuals, but governments acting in the name and on behalf of their electorates. In this case, it is a matter of reconciling not divergent individual utility functions, but divergent collective utility functions, which are determined by means of complex negotiation and compensation processes conducted by the various groups that help to elect the single governments.

To begin with, the monetary constitution basically involved a regime of flexible exchange rates, which enabled the European governments to keep its internal market separate, within limits, from the perturbations affecting the other European markets. But the adoption of flexible exchange rates made some governments tend to become rather benevolent on the matter of their internal inflationist processes and to use the tool of "competitive devaluation" as a means for improving their national balance of payments - and this opportunist behavior penalized the countries who were following a stricter line of conduct.

All this explains why someone suggested a regime of fixed exchange rates, or of rates fluctuating within clearly-defined upper and lower limits at least. Choosing fixed exchange rates or a snake was not, in itself, enough to make the governments of the countries with a weaker currency adopt a stricter behavior, however. These governments had to be "obliged" to embark on a course of great severity and the only way to do so was to assign the task of managing monetary policy to an independent outside authority, such as the European Central Bank. This idea is reminiscent of the legend of Ulysses, who orders that he be tied to the mast of his ship

so that he cannot give in to the sirens' song. In European monetary matters, the sirens embody the nations' propensity for inflation due to their high budget deficits, and the national governments are cast in the role of Ulysses. To prevent them from hearing him begging to be released, Ulysses made his sailors momentarily deaf. In the same way, the ECB was made deaf to the pleas of the national governments to avoid the bank giving in to their requests to loosen the constraints. Leaving aside the myth, we may wonder why - towards the end of the last century - the national governments of Europe agreed to a rule that they had looked on with some concern in the previous years.

The drive towards a single currency, with a single monetary policy inspired by strict principles is powered by a number of motives. There were geostrategic motives, in that the single European economies appeared too weak to cope with the new global competition. But there was also the idea that, in the long term, the single states' use of discretionary monetary policies would have failed to produce a durable effect on the single national economic systems. This change of view concerning monetary policy has certainly been influenced by the monetarist revolution, and there has also been strong pressure from Germany, which wanted a system of governance for monetary policy entirely similar to the one the country had used in the past.

Talking of the Euro enables us to see how the choice of one monetary regime rather than another, codified by international agreements, induces agents (governments) to act on behalf of principals (electors) who do not have enough information to understand the relationship between the available choices and their consequences. In the end, the agents rely for their information exclusively on the foremost theories concerning monetary policy, and the principals end up by taking for

granted the assumptions of the dominant economic school. In the case of the Euro, the agents agreed to throw in their lot with supply-side economics, with a consequent about-turn in the objectives of their economic policy. From the Keynesian goal of full employment, they switched to aiming for price stability, on which the objective of full employment is made to depend. The choice of the rule has been prompted mainly by factors of a political nature. The creation of a new constitution seems to be due to a change in what we could call collective preferences on the matter of economic policy.

### **Example II- From Collectivism to Liberalism**

A very “strong” example of the adoption of new economic constitutions emerges from the conversion of the collectivist economies of the countries in Eastern Europe (guided by the Soviet Union) and the Far East (guided by the China) into substantially market economies. In the case of Eastern Europe, the change of rules relating to the governance of the economy has clearly been accompanied by a change of rules relating to the governance of the countries’ politics too, i.e. in the Eastern European countries and the ex-Soviet Union (now Russia), the economic changes have coincided with changes in the political system, which has become largely liberal, or at least multi-party. In the ex-collectivist countries of the Far East, on the other hand, the economic liberalization and privatization process has not been accompanied by any significant changes in the political system.

The institutional solution chosen by China and the other Asian countries seems to be contradictory, because it is generally assumed that there *has to be* consistency between the economic system and the political system (Wu 2006). It has been noted, however, (Fan and Fan 2003) that China’s greater economic

success, by comparison with Russia, is probably thanks to a greater economic decentralization, to a sort of greater fiscal federalism. According to Fan and Fan (2003), this greater fiscal decentralization is accompanied by a more marked decentralization of power and decision-making. In Russia, on the other hand, the introduction of a multi-party system has not been accompanied by an adequate decentralization of power, probably due partly to the fear that this might accentuate the centrifugal tendencies of Russia’s peripheral regions.

In general terms, a change of economic regime like the one experienced by the ex-collectivist countries might be expected to give rise to a conflict at social level between different systems of rules. In Russia, the political anarchy that followed the fall of the old regime enabled rules inspired by a Mafia-like behavior to become established in many sectors of economic life. In China, the change to a new economic regime has been piloted by a political power that has kept a firm control over events, though, even there, there has been no shortage of signs of Mafia-like groups gaining ground.

Apart from Russia, the countries of Eastern Europe have charted a specific institutional course, in which the economic and political reforms have been strongly influenced by the will to join the European Union, which demands an alignment of their legislations with European standards (Altomonte 2005; Welfens et al 2006). For all of these countries, joining the European Union has become the fundamental objective function with which all other objectives must comply. The case of Eastern Germany is very particular, because it was assimilated into Federal Germany immediately after the fall of the Berlin wall. Going against the expectations of German policy-makers the homogenization process is experiencing

considerable difficulties due to the imbalance between the economies of western and eastern Germany. Among the various issues, there is one, immaterial asymmetry –i.e. the different attitude to entrepreneurial spirit that people generally exhibited in western and eastern Germany- the obvious consequence of which is represented by the higher levels of unemployment in eastern Germany than in western Germany.

### **Example III: Governance of International Migratory Processes**

The last 20 years have been marked by a strong increase in the migratory flows from very poor countries to richer nations and, according to many scholars, this is a phenomenon that seems destined to increase further, posing severe problems for the countries into which the greatest migratory flows are pouring.

Given the numbers involved in the phenomenon, it is easy to see that these problems concern both the stability of the economies of the countries of immigration and their political relations with the countries of emigration. The issues to consider include: a) the factors determining the migratory flows; b) the effects of the host countries' societies and the economies; c) the effect on the societies and economies of the countries that the immigrants have left behind; d) the policies implemented by the countries of immigration; e) international agreements for governing the phenomenon.

Calculating the quantitative dimensions of the international migratory phenomenon is by no means easy. Estimates have been attempted but they tend to underestimate the real dimensions because, in addition to the authorized immigrants, there are considerable numbers of unauthorized immigrants involved. However, it is worth noting that the forces driving international migration are fundamentally represented by the differential

in income and by the availability of information on said differential in income, combined with the fact that it has become much easier to travel from one country to another. The migratory flows are driven mainly by economic factors, to which we must add the migrations determined by political factors.

The areas absorbing the largest numbers of immigrants are the United States (where emigrants from Latin America tend to flow), Western Europe (where emigrants from Eastern Europe, Africa, the Middle East and Asia tend to flow. As for the economic and social effects of the countries of immigration, these depend primarily on the dimensions of the phenomenon, but in any case some effects are positive, while others are negative. From the economic standpoint, immigration can fill the gaps that develop particularly in all those jobs that are least satisfying and least well-paid. This explains why the GDP of countries of immigration can increase also thanks to the arrival of foreign workers (Borjas 1995).

The contraindication lies in that a strong influx of scarcely-qualified workers can sometimes give rise to a delay in the processes of specialization towards more qualified activities (Simon 2002). From a social and cultural point of view, immigration can lead to the creation of ethnic ghettos and an increase in crime rates (Hillman and Weiss 1999), thus incurring social costs that are not easy to quantify, but may certainly be considerable. There is also the fact that significant financial flows from the countries of immigration are generated by the money that immigrants send home. This is a cash flow that travels only one way, away from the countries of immigration.

As for the policies that countries of immigration strive to implement, there seems to be a general tendency to try to put a stop to unauthorized immigration and to select immigration flows that are consistent with the

needs of the growth of the host economies (Chiswick,2000). This selection is based on the immigrants' personal capital, but also on the compatibility of their social capital with that of the country of immigration. As a result of these general objectives, attempts are made to establish bilateral agreements with the immigrants' home countries, making them the destination of net financial flows and investments in exchange for their commitment to contrasting illegal immigration. The countries of emigration are not always in a position to control their frontiers, however, especially in terms of people heading out. In short, sizable flows of immigrants into the economically more advanced countries influence the development of rules for governing the local work market.

## Conclusion

The three examples discussed, i.e. the creation of the Euro, the transition from collectivist to market economies, and the development of massive migratory flows from one country to another, all demonstrate how the onset of particular phenomena at global level can drive changes in certain rules (some of them hugely important) for governing the economy. In fact, an attempt is made in each case to identify strategies that can be shared on a more ample, or even global level. So we must focus on analyzing the consistency between the economic and social phenomena dynamically taking place and the strategies adopted to respond to these phenomena in order to understand the emergence of new institutions, and of new constitutions in particular.

Some of these potential new constitutions are currently under construction. This is the case of a regime of international trade capable of obtaining the consent of the majority of the countries, irrespective of their relative position on the world market. This is also the case of the rules for governing intellectual

property rights that should bind governments to make efforts to combat forgeries and piracy, in accordance with those principles of loyalty that should underlie international transactions. The construction of consent and the creation of shared rules is taking place, albeit amidst a multitude of difficulties, within the context of the WTO (Anderson and Hoekman 2006).

This legitimately leads us to wonder about the new issues appearing on the global world horizon, some of the most important of which concern the management of the fundamental natural resources. Amongst these, the management of the energy resources and water resources come top of the list. At present, there are no rules shared at global level on how these fundamental resources should be managed and it is still impossible even to chart a course that will lead towards shared strategies on these issues. Unlike the case of international trade, where certain general principles appear to have become consolidated, there are absolutely no shared guiding principles concerning the world's energy and water resources- and yet these are issues on which it seems increasingly urgent to focus all the imagination of the builders of economic constitutions.

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## Corporatism

*Estrella Trincado*

### **Introduction**

The term Corporatism, used in an ideological sense, emerged in nineteenth century as a conservative alternative to the political pluralism and the idea of one person, one vote, of liberal democracies. Corporatism sought to give direct parliamentary representation to industrial groups, organised into employee and employer “corporations” that would negotiate income distribution between social classes. These corporations (industry councils in the US) were supposed to have rights, privileges and responsibilities distinct from those of their individual members. The political state would be no more than a third group in the social co-ordination process. In short, corporatism tried to respond to the problem of political participation by assuming social classes could exist in a gestalt framework, be they in harmony or in conflict.

Three types of corporatism could be identified: socialist, fascist and a more liberal corporatism. Since the Church has historically been one of the main historical corporate groups, some corporatist tendencies have also been based on Catholicism or personalism, which supposedly defended a more human-based society.

The roots of the idea of corporatism are social engineering. Socialist corporatism emphasises the harmony between social corporations and normally resorts to state intervention or public property to discipline market movements.

Fascist regimes advocated a group, non-universal and compulsory democracy, meant to maintain the status quo of elites through patrimonialism. This mode of corporatism had complex connotations besides the more immediate anti-liberal one. It was usually

related to nationalist ideology (nation as a corporation, a natural unity entrusted to leadership). Schmitter affirms that this corporatism, based on hierarchical, functional and non-competitive categories was a structural response to the Depression, not an ideology in its own right (Schmitter 1979a).

More recently, a liberal regimes corporatism claims to embody a more direct and consensual democracy through the governance of large corporations. Social demands are expected to be transmitted through certain functional associations, which are bestowed with a monopoly of representation. This monopoly is justified by the greater social significance of the associations and by the difficulty of putting direct democracy into practice in a globalised and complex society.

Nevertheless, over the years the term corporatism has defined a variety of ideas, not all of them mutually compatible (see Williamson 1985) and interest in this ideology has led to countless publications. Sometimes, the term is used contemptuously to refer to the tendency in our globalised society of large companies to increase their power at the expense of political states. Critics object to the way firms obtain their information since sometimes they have more extensive and detailed databases of their consumers than the government itself. Finally, the term corporatism is used to refer to endogamic tendencies peculiar to non-individualist societies, based on entrepreneurial or extended family group relationships.

### **Historical Antecedents of Economic Ideology**

The Latin corpus, or corporation, refers to the existence of a group or collective body, which constitutes an entity distinct from that of its members, with a mind of its own. From time immemorial, philosophers like Plato, Albertus

Magnus, who defended a corporative just price, or Aquinas have claimed the existence of corpus. But the mercantilists and historicists stressed, above all, the importance of corporations, considering them the “productive force” that granted impulse and direction to future production. They reacted against the cosmopolitanism and individualism that, according to them, broke the ties that bound men together.

The Methodenstreit argument between the “Younger” Historical School and Austrian School can be summed up as follows: the former held the conviction that society is set up as a collection of organic institutions; the latter believed society was a set of atomistic institutions, product of the invisible hand that leads the individual interest to the common good. Leading members of the last generation of German Historical School, Werner Sombart or Max Weber, initiated an alternative school of thought in which capitalism is not reduced to the idea of competitive markets but rather is considered to be a wide range of social institutions and processes.

Also, institutionalism describes economic laws as products of a collection of organic institutions, perpetually changing. Social organisms are like biological entities that grow and mature, whose components become mutually dependent and whose life is longer than the lives of its parts. Saint-Simon also believed in the “spontaneous harmony” of the “organism” of industrial society.

The organic approach to philosophical and social problems contrasts with the individualistic approach. Often, it is based on Hegel’s idealist philosophy and von Savigny’s organic jurisprudence and thus disagrees with Locke’s individualistic philosophy and jurisprudence. In fact, Hegel defined freedom in terms of corporations (Church, family, State), whereas Locke

defined it as a relationship between the individual and the group.

### **Socialist Corporatism**

The corporatism of pre-industrial societies was based on a harmonic vision rather than the negative social consequences of capitalism. In the nineteenth century, nevertheless, it grew out of a reaction to liberalism and the Industrial Revolution, and out of mistrust in the “anarchic” forces of market. After the French Revolution, socialist and Catholic tendencies emerged that bemoaned the disappearance of the former medieval guilds. In this age, corporatism was included especially in the social Catholic movement, with theorists like Frederic Ozanam, Albert de Mun and Henri de la Tour du Pin in France; the group of Magunida in Germany; and the Viennese School in Austria. Pryor (1988) deals with the roots of the idea of corporatism reaching back into the nineteenth century, when the Roman Catholic Church was its main source.

### **Fascist Corporatism**

However, in the twentieth century, in the interwar period, the use of this word was widespread in fascist movements, especially in Italy where they tried to build a “Corporative State” in the fascist sense of the term, as opposed to free unionism (O’Sullivan & Cox, 1988). This concept is connected to the idea of “Aesthetic State” and the mysticism of the Political State. Aesthetics represents the instinctive part of human beings and is the symbol of cooperation between all their impulses and needs. Based on the ancient idea of corpus, some fascisms built systems around races instead of individuals, with an antirational mythology and a social Darwinist scientific spirit as their framework. They assumed that private firms emerged as an environmental adaptation where free trade and state intervention

coexist. The government and the main corporations must be in charge of selecting the more adaptive enterprises and supporting them, getting rid of the less adaptive competitors. States should have the ultimate authority over production and distribution without possessing the means of production and distribution. So, they have to achieve a policy of collective bargaining and cartelisation in order to have representatives of social groups in councils that could implement planning of economic policies.

Italian fascists (Giuseppe Bottai, Benito Mussolini, Affredo Rocco or Edmondo Rossoni) tried a corporatism in which capital and labour were divided in “chambers” controlled by the State. The Duce’s statement that red “Fascism is corporatism” has become famous. The April 3, 1926, Rocco Law forbade free unions and strikes and created a system of compulsory unions that represented the three groups involved in the firm – employees, employers and the officials of Fascist Party. An economic system organised by the producers themselves, under the direction and control of the State, was envisaged. The collaboration and solidarity of the different production factors would achieve the stated goal of attaining national prosperity and grandeur. With this justification, the only legal unions were those whose leaders were Italians with no ties to international associations. Also, the system nurtured an open state paternalism and protectionism.

In the interwar period, a corporatism movement appeared in Rumania, with Manilescu at the forefront. In France, corporatism was connected with offshoots of the socialist sector. While Pétain was in power, his policies seemed to approach corporatist tendencies in agrarian and industrial sectors. It was also defended from natural law and personalist philosophical points of view, like Maritain’s, who envisaged a democratic world federation of

political societies, based on the leadership of a multiplicity of civic fraternities. In this period, 1931 Pius’ XI Encyclical, *Quadragesimo Anno*, presented a Church Doctrine that also defended a corporatist structure, similar to that of Italian Fascism (Pollard, 1985), and in accordance to 1891 Leo’s XIII Encyclical, *Rerum Novarum*, which emphasised harmony between all social groups.

Corporatism was also of great importance in the Spain of the dictatorships of Primo de Rivera and Francisco Franco, with its so-called “*Nacional Sindicalismo*”. In this case, the idea was continued by the traditionalists of social Catholicism, whose political branch was the Falange, a movement nostalgic for medieval society, which Falangists assumed lacked social conflicts. This corporatism is related to syndicalism, as the state is supposed to be eventually replaced by a federation of unions based on functional economic organisation instead of geographic representation. Corporatism also appeared in Portugal, with Salazar, in Austria, with Dolfuss and Schuschnigg and in Argentina, with Peron.

Schmitter (1979b) considers that corporatism in Spain and Portugal was a response of the landowners and bourgeois to the menace of modernisation and industrialisation and to proletarian power. On the other hand, Wiarda (1973, 1997) rejects the idea that corporatism was a product of class interests. Culture and tradition created corporative structures as a response to the crisis between the state and civil society. (For further debate see Bastien & Cardosa 2006; Almodovar & Cardosa 2005.)

### **“Liberal” Corporatism**

At times of economic crisis and lack of social cohesion, the idea of involving representatives of interest groups (especially unions and employers associations) in



government politics, above all the labour policies, re-emerges. This policy implies an increasing polarisation of social groups. It is usually called neo-corporatism (term created by Philippe C. Schmitter), income policy or neo-contractualism.

In fact, new forms of corporatism have been tried in the liberal democracies. For example, in twentieth century Japan, government had a close link with the entrepreneurial world and crises were overcome, not by union power, but rather by the concentration of power in a few "Zaibatsu" that had important interconnections with financial entities through a corporative capitalism (Shigeto, 1993). In Austria, as in Switzerland, since World War II a state corporatism has developed in which government and corporations have reached a consensus (Katzenstein 1984). In Sweden, with the Saltsjobaden Agreement, in 1938, between S.A.F (employers' association) and L.O. (the major Swedish blue-collar Union Confederation), the role of government had less importance. A labour market council was created, precisely with the idea of avoiding the labour legislation and setting up rules regulating layoffs in the context of cooperation. That led to a greater influence of unions over workers and, according to Pekkarinen (1992), until 1970 central bargaining worked well. The same applies to Scandinavia and the Netherlands.

In the 60's and 70's in Great Britain, unions, capitalists and government tried to implement wage and price control policies (Harrison, 1984). Western European Social democracy and Christian democracy created "works councils" to meet employees and employers together. In Italy, the Scotti Agreement, January 22, 1983, was based on the industrial relations of the corporative system. In Spain, income policies of the period of transition to democracy (Pactos de

la Moncloa 1978), constituted a type of corporatism based on social agreements (Foweraker 1987).

The Common Agricultural Programme of European Union is said to be influenced by the corporative tendencies of French farmers or by Dutch corporatist policies. Some consider the institutional structure of Germany, which encourages the negotiated approach, as a type of corporatism. This policy based on labour agreements was less workable in Germany after the early '80s but has recently been revived with the recent tripartite Alliances for Jobs (Berger 1981).

Corporatism has a long history, not only in Europe, but also in such different places as China (Chan and Unger 1995), or Latin America, where corporative representation has increased and has been very useful in maintaining social peace. Brazil still suffers from the 1930s corporatism of Getúlio Vargas (Erickson 1971), which is yet defended by the Brazilian President-elect Luis Inacio da Silva (Lula). This tradition also persists in Argentina (Murillo 1997), Mexico (with the PRI, see Grayson 1997), Chile (especially with Pinochet, see Silva 1996), Bolivia (with the MNR), Guatemala or Ecuador (for classic perspectives on Latin America corporatism, see Malloy 1977; for a comparative analysis, Collier & Collier 1991). This reality makes Latin American market liberalisation very difficult, due to the political control of corporations.

### **Pros and Cons of Corporatist Tendencies**

Criticism of corporatist tendencies has been a central part of economic analysis since Adam Smith's assertion in *The Wealth of Nations* (I.x.c.31): "The pretence that corporations are necessary for the better government of the trade, is without any foundation. The real and effectual discipline which is exercised over a workman, is not that of his corporation, but that of his customers". Many others have

criticised corporatist possibilities of capitalism: one example is Karl Marx, another is the gradualist socialism of the Fabian Society, which considered the increasingly monopolistic character of capitalism its main chronic problem because it placed capitalism out of accord with public interest and democracy. Fabians not only had influence in British Labourism: Keynes took his defence of the state assuming the task of “concerted and deliberate management” from the Fabians. In this line, although with Marxian touches, Kalecki based scientific method on social classes in the corporative sense. Sweezy presented US “neocapitalism” as a rational planning by the state in close partnership with Big Business and organised labour.

Furthermore, Schumpeter foresaw that competitive capitalism would become a trust-based one. As businesses work like oligarchic states, whose voters are shareholders, political conceptions that justify state intervention and central planning are justified. Galbraith stressed the disappearance of the competitive world in the US because of the monopolistic situation of enterprises. Emergent “countervailing powers” in the form of trade unions, supplier and consumer organizations and government regulation will balance the concentration of corporate power. Radical Economics and American pragmatism have also presented criticism in this direction, based on historical and American institutionalism tendencies.

Karl Polanyi denounced the “disembeddedness” of capitalist structures in other non-economic institutions. As capitalism is not organised along the lines of social relations, it erodes the quality of human existence and needs artificial “agreements” to sustain itself. Polanyi’s alternative existential substantivism presents the market process as a “double movement” of reification - resistance to the lack of “reality of society”. A

somewhat opposite view is presented in Granovetter (1985), who emphasises the networks of interpersonal relations and the embeddedness of contemporary capitalist societies.

In the so-called New Economic Sociology the notion of embeddedness has been used to offset the neo-classical principle of social atomisation. Much of this work has tried to understand human action within the framework of established capitalist institutions and corporations. The recent theories of “Social Capital”, and political or organisational capital, are also based on these concepts. Liberal society and representative democracies have been challenged, as they are believed to have led to an erosion of citizens’ participation and of social bonds of trust. The resources inherent in social relations facilitate collective action and encourage bargaining, compromise, and pluralistic politics and the formation of crosscutting groups (for a comparative analysis of the alleged decline of social capital see Putnam 2002).

There are some who say that the society we live in is more a corporatist society than a capitalist one. That implies according to Locke (2002) that we are looking at socialism for the bourgeois, since we enjoy private property and the management of enterprises while the government guarantees a flow of material goods to its constituents. Besides, corporatism gives a response to critical governance issues and, at the same time, creates its own governance problems. Andersson (2000) points out that the corporatist model is not an efficient means of social organization in the globalised economy given it produces poorer results of production and employment. Corporatism produces unemployment (Newell & Symons 1987) and, as a result, Chalmers foresaw its eventual disappearance in its present form (Chalmers 1985). Besides, neo-corporatism seems to

create new and unknown problems (see Grant 1985). For example, international organizations lack evident control and jurisdiction over trans-national questions, and it is debatable whether civil society organizations (NGOs) are as representative as national trade unions (Ottaway 2001)

Nevertheless, in opposition to the criticism of entrepreneurial corporatism, in 1999, Davos World Economic Forum, UN general secretary Kofi Annan proposed a “global compact” between firms and civil society to face environmental or human rights problems. He hinted about a tripartite model of “global corporatism”—international organizations, civil society (NGOs and labour unions) and enterprises—and the extension of bureaucratic structures, through “partnership” (Ottaway 2001). In 1999-2000, the “Vision Project on Global Public Policy Networks” of UN also proposed corporatism as a system to fill the “governance gaps” of the UN.

### **Visible Hand Recent Criticisms**

With the increasing reach of the “visible hand”, long ago in the US a debate emerged in which one side pointed out the benefits of administrative coordination and the other denounced the increasing socialist tendency of the economy, where individuals lose their power and control and where vertical integration creates more and more bureaucratic governance. According to Douglass North, these negative processes are produced by endogenous cognitive changes.

Corporation problems are studied through interest groups and rent-seeking methodology, through an insider-outsider perspective, or studying transaction or information costs. In Mueller (2003) a thorough study of these methodologies can be found. The danger of the government falling under the influence of interests not compatible with the general welfare is implicit in corporate power. According to

Olson, once the large initial costs of organisation have been overcome, many groups turn to other ends, of benefit to their members, but different from their original objectives. Also, large groups are more difficult to organise and require incentives to curb free-riding behaviour. This fact explains why in poor countries, where the agricultural sector is large, farmers receive small subsidies for their products, whereas in developed countries it receives giant subsidies (Mueller 2003:475).

Moreover, when the government helps create a group’s monopoly position, potential monopolists will invest resources to increase the probability of obtaining the monopoly. An additional social waste, different from the traditional cost of monopoly, would emerge in the form of transaction costs, lobbying fees and time and money wasted on the bureaucrats’ competition for monopolistic power. When non-free entry is guaranteed, these costs do not dissipate the monopoly’s income (Mueller 2003:338).

Several studies have attempted to relate interest group strength to government size or to the development of political business cycles. Besides, Thurow affirms that asymmetric information causes a breakdown in the functioning of the market in the corporative world. Individual agents do not have the same opportunities as corporative or institutional agents. Corporations are becoming larger and larger because their size increases the visibility of the entrepreneurial value.

Since the early 1990s, Europe in particular has tried to avoid corporative tendencies. In England, the Cadbury Report (1992) was the first code of fair governance that was used as a model for British firms and for the subsequent European codes (e.g., French, Spanish). It tries to control executives, who are considered to have acquired too much power. Debate over corporatism in US has

been more intense since Microsoft was charged in 1997 with having broken US antitrust law. Monopoly dangers have been defined and its boundaries established. Policies have been proposed to re-regulate areas previously deregulated.

Critics have also compared US policies that aid large firms in danger of bankruptcy, especially in the defence industry, as a type of fascist corporatism. The debate has increased even more with the Enron bankruptcy proceedings in the early-mid 2000s, previously considered a symbol of innovative management. The issue of corporate governance has become a major theoretical and practical legal concern after subsequent corporate scandals and bankruptcies of large enterprises and auditing agencies. Principal-agent theory shows that the division of power between business executives and shareholders leads to a lack of representation of shareholders' power on administrative boards, which is an emerging corporate tendency. Nevertheless, Merton (2003) says that regulation restrains financial evolution and that no punitive measure can avoid a lack of business ethics in the corporative system. Market complexity makes internal or external controls increasingly difficult.

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## Critical Realist Governance

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Initially emerging out of the work of Roy Bhaskar (1975,1979) in the 1970s, Critical Realism is a position in philosophy that attracted attention because of its close critique of the contradictions of strong social constructionism and postmodernism and because of its appeal to Marxists in providing an alternative to positivism (Brown, Fleetwood, Roberts 2002). It has influenced the work of prominent social theorists, such as Andrew Sayer (1992,2000) and Margaret Archer (1995,2000), well-known socialist thinkers, such as Andrew Collier (1989,1990,2003) as well as political economists, such as Bob Jessop (1997,2003), and has a growing influence as a model for social science in disciplines such as economics, through, for example, the work of Tony Lawson (1997, 2003).

Governance loosely defined as the design of institutions and organisations for making and implementing collective decisions (Burki and Perry, 1998), is far broader than the traditional view of the constitution of politics or economics. Several features of Critical Realism make it a powerful analytical tool with which to explore this breadth.

### **Causal Complexity of Open Systems**

In social science, Critical Realism focuses on the central problem of the causal complexes that contribute to events. It provides a solution to the longstanding problem of the relation between structures and agents. The activity of agents occurs in terms of constraining and enabling structures (formal institutions, social relations, enduring rule systems etc.) and that activity reproduces and transforms those structures. Structures occur in overlapping ensembles and also in stratified relationships, because some

structures, such as the United Nations presuppose others, such as the prior existence of states – with all that that might entail (Wendt 1999). Critical Realism, therefore, is useful in foregrounding the complex inter-relationships of systems. It places great weight on the production of events and decision making as active processes by a broad constituency of participants. At the same time it doesn't lose sight of the way those events and decisions are crucially shaped by the prior conditions in which participants find themselves. Causation is a matter of the confluence between thinking agents and structures. Events are multiply determined and contingent implying that things could always be otherwise and that systems are open rather than closed sets of regularised outcomes. However, that certain outcomes are more likely and often recur within systems entails that structures are genuinely separable from agency, providing a real constraint upon it. The typical interplay of agency and structures reproduces its own conditions and generates systemic tendencies. Causation is therefore not of the Humean variety 'whenever A then always B' but rather the characteristic ways of operating of a given confluence. Agents are not always fully cognisant of the full significance of all aspects of the system within which their activity occurs and to which that activity contributes. Accordingly, Critical Realists conceptualise reality as something with 'depth'—systems have duration in terms of the structural ensembles (rules, institutions, operations etc.) within which agents act to produce events of which they have some fallible interpretation and on the basis of which they proceed. Reality is therefore analytically split into structures, events, and human experience of events. Change is a matter of critically appraising how systems work on the basis of the effects of structures and how agents reproduce them and how we



might work to better them. In his work on democratic global governance Heikki Patomäki captures this well (2003:10):

A vision of global democratisation would have to be grounded on realist analysis of the relevant context, its concrete embodied actors, its social relations and mechanisms, and its real transformative possibilities. Without appropriate understanding of a particular context, and explanation of the relevant outcomes in a critical way, it is impossible to know whether any change is needed and if yes, what kind. Abstract blueprints, detached from realities won't do.

### **Illustrations of Critical Realism**

Critical Realism is not a dogma. It does not prescribe a particular method of empirical analysis. It is rather conducive to a variety of foci. One might for example, explore the contribution of a single strand to a causally complex event, and one might work outwards to broader systemic conditions.

#### *(A) East Asian Financial crisis of 1997*

Realist analysis, for example, can be used to explore how knowledge or discourse is a causal constituent in crises of global governance. The East Asian financial crisis of 1997 was intimately related to pressures for deregulation of financial markets (Morgan, 2003). Some of the authority for that pressure derived from World Bank research. The 1993 *East Asian Economic Miracle* report applied a total factor productivity model to establish that the principal source of growth in East Asia resulted from improvements in technology and labour skills in highly competitive product export markets where competition deterred any state intervention from taking forms that would work against market forces. The key role of state intervention in encouraging supply through anticipating and identifying demand areas

was thereby under-emphasised. At the same time, the research supported the view that more and freer investment would enhance growth potential. The capacity of any particular real economy to absorb additional capital smoothly was not considered (since the models used absorbed capital smoothly); nor was there a distinction made between governance issues to deter short-term speculative investment to exploit margins and long-term investment initiatives tied to the enduring success of any particular scheme. The results of this deregulatory pressure are now well documented, as are the results of the loan conditionality stipulations of the subsequent IMF intervention. Standard IMF governance policies such as higher interest rates and cuts in government spending simply pushed up the burden of servicing debts held in dollars and prevented the various states from supporting firms that were currently illiquid but not necessarily long-term insolvent. The number of bankruptcies was thereby increased and due to the flying geese model of sub-contraction, the crisis was exported throughout the region on the demand side, as well as through the collapse in confidence in their financial systems.

Behind both the research that contributed to the pressure for deregulation and the governance response of the IMF stands orthodox economic methodology. That methodology abstracts from the complexity of real economies to model them on the basis of highly stylised mathematics that assume systems are closed patterns of regularised behaviour based on a Humean notion of event regularity causation (Fleetwood 2002). Critical Realists argue that orthodox economics is unrealistic but has real and damaging consequences through the authority it lends to global governance organisations and policy. In this instance, poor governance and poor economics are mutually reinforcing. Economists are agents who work according to

the constraining and enabling structures of the discipline of economics (Lee and Harley, 1998). The socialisation of the mainstream produces characteristic ways of theorising that many orthodox economists themselves have become uncomfortable with but continue to reproduce. The World Bank and the IMF continue to select their staff economists from this pool and this arguably has undermined any substantive shift in the fundamentals of the economics from the Washington to post-Washington consensus (Wade, 2002; Fine, 2000).

*(B) Broader Conditions of Financial System*

In *Democratising Globalisation* Patomäki (2001; see also Grieve, 1999) explores the relatively weak governance of the global financial system from a Critical Realist perspective. Since the 1970s there have been over 70 banking crises and 90 currency crises indicating that the system is causally conducive to escalating instabilities. Deregulation and, as new technology has allowed, the growth in the number of tradable financial instruments in increasingly integrated national financial markets has increased the volatility of the system. Derivatives, for example, were initially introduced as a way of stabilising long-term prices since their trade was supposed to produce a self-fulfilling convergence of expectations and allow 'risks' to be offset (Morgan, 2003b). However, without stronger regulation the market is fundamentally vulnerable in terms of both its structure and the characteristic activity of financial agents. Debt ratios and the leverage of firms that deal in financial instruments such as derivatives can be extremely high (several times their initial capitalisation). Firms tend to trade across each other and regions and thus produce mutual dependencies and lines of transmission. Different traders behaviour tends to converge in particular markets quite

quickly. A principle reason for this is that the efficiency of traders is measured in terms of their deviation around the average returns of the market and thus of other traders. Identifying and following market trends, and being receptive to their shifts, rather than cutting against them, therefore increases job security. As a result the inherent uncertainty of events can produce massive sudden shifts in trader behaviour, producing either bubbles (escalating prices) or sudden crises. The Enron scandal is a classic example of how derivatives can be destabilising when traders are able to manipulate the market (in this case the US power market) to which derivatives relate. Such an unpredictable event can serve as a trigger for rapid shifts in expectations that sweep through the financial system precisely because financial actors tend to converge in their behaviour and the systems are so integrated across different kinds of financial markets and across regions.

From a Critical Realist perspective the basis of the financial system tends to be misunderstood. Orthodox economics, for example, assumes that the volatility of financial markets, particularly foreign exchange or FOREX markets, reflects problems with the economic fundamentals of the economy. It pays insufficient attention to the real causal powers of the emergent causal complexity of the financial system to work in the opposite direction. Since current thinking is based on the idea that free markets produce optimal outcomes orthodox governance solutions tend to be weak attempts to stabilise confidence as a way of modifying sudden changes in behaviour. For example, a typical response to the exponential rise in FOREX trade has been for central banks to increase their reserves in order to assure traders that they can effectively intervene to stabilise currency prices in the event of a run. This approach is self-defeating and reactive. On the one hand, the rate of increase in FOREX



trading outstrips the capacity of central banks to increase their reserves in a credible way. On the other hand, such a policy is always playing catch-up rather than addressing the basic determinants of volatility.

### **Governance Transformation and Reform**

A central characteristic of Critical Realism is that working to better our conditions of existence is a necessary outcome of good explanation. Bhaskar in *Scientific Realism and Human Emancipation*, expresses this as (1986:184):

“The empirical establishment of theory T shows belief P about object O to be false (illusory, inadequate, misleading), whose inference is a negative evaluation of the status of O in terms of its relations to P and a positive evaluation of action directed at the removal of that relation as a transformation of O.”

In simpler terms, better explanations of events and their grounds provides the potential for understanding that in itself changes our behaviour, and thus the way we reproduce structures and make systems, and also points to rational alternative possibilities that overcome problematic aspects of systems. Through the NGO *Network Institute for Global Democratisation* Patomäki (2003, and with Teivainan, 2002 and 2003) has, for example, been involved in exploring various global governance policy reform initiatives. One important innovation that received attention at the World Social Forum 2003 has been a *Draft Treaty on Global Currency Transactions Tax* (2002). The treaty is designed to produce an operative institutional form of the small currency transaction tax first suggested by the economist James Tobin in 1978 and since championed by the NGO ATTAC (Morgan, 2003c). If factored into the computer systems through which FOREX transactions are routinely made the tax has a number of advantages. It becomes part of the

overall calculation of margins. As such it is highly transparent within the system, becoming an immediate part of the trade decision. In time of high volatility it could entail well-publicised progressive levels that would act as an automatic stabiliser in a way that central bank interventions to buy up currency cannot easily do because of the volumes of trade. Since it is inserted into the technology of the already existing system of trade its costs of collection would be extremely low and its avoidance unlikely. Since it can be adopted on an ad hoc basis from individual national trading systems as they are keyed into the global financial system, it can gain a critical mass of participant countries without relying on initial sponsorship from states unlikely to endorse it such as the USA and UK. Furthermore, the revenue generated from the tax, if administered outside the Bretton Woods institutions, could provide the potential for aid in debt reduction for a number of states that find it extremely difficult to avoid the onerous governance stipulations of the IMF precisely because of their debt reliance. It could therefore, be a trigger, for a more democratic and accountable form of global governance that builds concretely on the World Social Forum credo that “Another world is possible”.

### **Conclusion**

To summarise, Critical Realism is one useful way of bringing together a number of elements that are all too often separated. It provides concepts for the philosophical analysis of the underlying assumptions of theory, such as economics, in order to identify possible ontological deficiencies, such as a reliance on closed system modelling or event regularity causation. It provides an open system alternative that can be applied to the empirical exploration of real world events. It can therefore be used to explain the

underlying tendencies of a particular social entity, such as the tendency to crisis within the global financial system, based on its current characteristics and weak governance. Finally, it places great emphasis on using explanation to reconstruct systems that build practically from critique. It therefore brings together philosophy, applied social science, and a genuine ethical commitment. In a governance context it is an example of synthesis that MacIntyre expresses as (1990:61):

“There ought not to be two histories, one of political and moral action and one of political and moral theorizing, because there were not two pasts, one populated by actions, the other only by theories. Every action is the bearer and expression of more or less theory-laden beliefs and concepts; every piece of theorizing and every expression of belief is a political and moral action.”

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## Eastern and Central European Politics and Policies

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### **Introduction**

Almost a generation after the collapse of the Berlin Wall and the dissolution of the Soviet Union, the legacies of communist rule continue to distinguish Europe's central and eastern regions from its western ones. Though definitions differ, European countries that formerly were part of the Soviet Union are now usually termed East European, while European countries that were ruled by communist regimes but were outside the Soviet Union are now usually termed Central European. Eastern Europe thus includes Armenia, Azerbaijan, Belarus, Estonia, Georgia, Latvia, Lithuania, Moldova, Russia, and Ukraine, while Central Europe includes Albania, Bosnia-Herzegovina, Bulgaria, Croatia, the Czech Republic, Hungary, Macedonia, Poland, Romania, Serbia and Montenegro, Slovakia, and Slovenia. Of the East European states, all but the Baltic states (Estonia, Latvia and Lithuania) were under communist rule for a roughly 74-year period running from the Russian Revolution of 1917 until the dissolution of the Soviet Union in December 1991. The Baltic states were under communist rule only following their forcible incorporation into the USSR in 1940. The Central European states were ruled by communist regimes for a roughly 45-year period lasting from the mid- to late 1940s to 1989 or 1990. In 2004, eight of the Central European and Baltic states entered the European Union, leading some to argue that they now have more in common with Western Europe than with the rest of Central and Eastern Europe. This article will show that there are indeed important differences across post-communist Europe, most commonly between Central Europe (and often the

Baltics) on the one hand and Eastern Europe on the other. But it will also show that post-communist countries remain similar in important ways. Overall, communist legacies remain profound enough even in the new EU member-states to justify continued consideration of all of post-communist Central and Eastern Europe as a single region of analytical interest.

Among the most popular subjects of interest in the study of Central and Eastern Europe are political parties and public policies. Political parties are among the most prominent political institutions of our time, found in virtually all democratic and non-democratic countries of the world. Perhaps the best overall definition describes the political party as "any political group identified by an official label that presents at elections, and is capable of placing through elections (free or nonfree), candidates for public office" (Sartori 1976:63). The virtue of this definition is that it draws attention to the most fundamental and distinctive task carried out by parties: they, more than other institutions, see to it that public offices are filled. Public policies are actions taken by governments to address problems arising in their polities, economies, or societies (see Kraft & Furlong 2004:4). Governments in post-communist Europe have faced more than their share of problems and have had to devise a range of policies to deal with them.

The countries of Central and Eastern Europe have become valuable case studies in the comparative study of political parties and public policies. This is due to at least three important factors: (1) the degree of change experienced in the region, (2) the similarities of communist rule across the region, and (3) the number of countries involved. The change was twofold, involving not only political but also economic transition. Moreover, change was unusually deep and wide-ranging, thanks to the extraordinarily pervasive reach of the

communist states of the region into their countries' political, economic, social, and cultural lives. Moving from monopolistic communist political control to what in most states has become a far more pluralistic (if not always democratic) political system has meant the creation and development of wholly new political parties and the creation and implementation of wholly new public policies. Moving from a command to a market economy has been equally dramatic. Although a past overemphasis on the homogeneity of communist regimes has been justly criticized, the similarities in communist rule across the region are undeniable, particularly when communist rule is compared to other forms of political rule around the world. These similarities, which spring both from a region-wide reliance by all regimes on a common Marxist theoretical canon and from Soviet efforts to maintain systematic control over its satellite states, provide an unusually common starting point from which to explain evolving differences in post-communist outcomes of political development. The relatively large number of countries involved—twenty-two at present—has allowed research on parties and policies to take on a truly comparative perspective. Given that parties and policies touch on a very wide range of political issues, research on both has also contributed to our understanding of many related topics. Among these topics are democratization, relationships among the executive, legislature and judiciary, the rule of law, transitional and emerging economies, and economic integration.

### **Parties as Political Institutions**

Parties are political institutions, but they are institutions whose relationship to the state varies depending upon the type of political system they inhabit. In democracies—those systems characterized by free contestation for

public office, open public participation in elections, and the protection of civil and political liberties (Lipset 1995)—parties are explicitly political organizations but not formal organs of the state. In non-democratic systems, ruling parties can become hard to distinguish from formal state organs. In communist non-democratic systems, ruling parties tend to dominate the state. Central and Eastern Europe has experienced a wide range of political systems in recent decades. The political parties of the region thus have taken on a variety of political roles.

As institutions, parties are organizations having particular structures, goals, and behaviors. While it can be useful to study parties individually, it is also important to recognize that their structures, goals, and behaviors are influenced in important ways by competing parties wherever more than one political party is permitted to operate. For that reason, the parties of post-communist Central and Eastern Europe are best studied not as individual entities but as components of country-wide party systems. Sartori's definition of party system, as "the system of interactions resulting from inter-party competition" (1976:44), nicely captures the key advantage of studying parties as components of their countries' party systems. Only when the actions and reactions of competing parties are taken into account can any given party be well understood.

Perhaps the single most important fact about party politics in today's Central and Eastern Europe is that the transition from communist rule tended to transform single-party systems into multiparty ones. In communist systems, political power is monopolized by parties formally dedicated to Marxist-Leninist goals. In most communist Central and Eastern European states, this meant that the ruling communist party was the only legal party. In some communist states, such as Poland and Czechoslovakia,

other previously non-communist parties were allowed to survive into and through the communist era. These satellite parties, however, only created the illusion of competitive politics; they persisted only because they forswore any further opposition to communist policies. When communist rule ended in Central and Eastern Europe, all countries developed multiparty systems. But while multiparty systems are inherently more competitive than single-party ones, they are by no means equally competitive.

The degree of competition seen in the multiparty systems of post-communist Europe varies across countries according to how well democratic politics has become entrenched. In some of these countries (Poland, the Czech Republic, Hungary, Slovenia, and Estonia, for example), multiparty systems have been truly competitive from the very start of the post-communist era, because they have operated in consistently democratic political environments. In other countries of the region (such as Russia, Ukraine, Georgia, Slovakia, and most former Yugoslav states), multiparty systems have not always been competitive, because they have operated for at least some periods of time under less than fully democratic political conditions. In some countries of the region (such as Belarus and Azerbaijan), multiparty systems exist but are hardly competitive at all, because elections are rigged in favor of ruling parties and opposition parties are systematically harassed. On balance, then, multiparty politics has become the new norm in Central and Eastern Europe, as it has in recent years in most countries of the world. But multiparty politics has not always meant fully competitive party politics.

Multiparty systems can also be analyzed according to the number of parties they have. In many Central and East European states, the long dominance of communist and (where applicable) communist-satellite parties was

initially challenged by single broad-based movement-parties whose diverse elements were united only by their opposition to communist rule (Batt 1991:ch 3; White, Gill, and Slider 1993:ch 8). Examples of such movement-parties are Solidarity in Poland, the Czech Civic Forum and the Slovak Public against Violence in the former Czechoslovakia, the Union of Democratic Forces (UDF) in Bulgaria, the Estonian Popular Front, the Latvian Popular Front, Sajudis in Lithuania, and Rukh in Ukraine. Most of these movement-parties soon disintegrated into competing smaller factions and parties once the common goal of ending communist rule had been achieved (the UDF, still an important Bulgarian party, is a notable counter-example). This ushered in a new period of party proliferation, in which various groups struggled to establish themselves as lasting political parties. While the most dramatic period of party proliferation seems to have passed in many countries, the overall number of parties remains high. Cross-national quantitative analysis of fragmentation, which considers the division of party systems by looking at the number of parties they have, suggests that post-communist party systems continue to have higher numbers of parties than more established party systems do. In an unusually comprehensive 2001 analysis that considered twenty of the twenty-two Central and East European countries, Central and East European party systems averaged 5.37 parties, compared to 4.21 parties for Western Europe (Birch 2001:359-360).

Another way to judge party systems is by the degree of stability they exhibit. Party system stability is sometimes measured quantitatively (Toole 2000, Ishiyama 2001) but is more commonly evaluated in qualitative terms. Among the indicators of party system stability are (1) that parties are devoted more to some coherent ideological

agenda than to the promotion of any one political figure, (2) that the roster of parties in a system remains constant, and (3) that ideological polarization does not unduly undermine the effective operation of government.

Parties devoted more to the promotion of an individual politician than to a coherent ideological agenda are often known as personalistic parties. They destabilize party politics because they tend to last no longer than their sponsor's popularity. With important exceptions, these parties are more common in Eastern than in Central Europe. The personalization of party politics has been a particular impediment to party development in Russia. United Russia, the main pillar of President Vladimir Putin's parliamentary support, is in part a successor to Unity, the party that previously had supported President Boris Yeltsin. Likewise, the nationalist Liberal Democratic Party (LDP) has long been a vehicle of Vladimir Zhirinovsky's political ambitions. Highly personalized parties also have played important roles in the party systems of Ukraine, Georgia, Armenia, and Azerbaijan. An interesting and relatively new subcategory of the personalized party includes parties centered on a country's former or potential monarch (Bulgaria's Simeon II National Movement and Albania's Movement for National Development). Researchers on Russia disagree on the causes and implications of its personalistic party politics; some have blamed the weakness of Russia's parties on Russia's unusual concentration of presidential power (Fish 2000, Rose 2001), while others claim that the blame lies mainly elsewhere (Ishiyama and Kennedy 2001). Additional research, and particularly cross-national research looking within and beyond the former Soviet Union, would help us to better understand this prominent manifestation of post-communist party system instability.

In many of the region's party systems, high turnover in the roster of parties remains a problem. Parties of all sizes emerge and disappear with a regularity not normally seen in better-established party systems. High turnover among at least smaller parties has been common in countries such as Russia, Ukraine, Poland, and Latvia. And larger parties are not immune; Estonia's Res Publica and Latvia's New Era are only two of the important parties to have formed and done very well in elections since 2000. Party systems with consistently low turnover rates are fairly rare, and of those the Hungarian provides the most extreme example. In Hungary, an unusually reformist communist regime allowed opposition movements to form prior to the end of communist rule, helping a diverse half-dozen parties to establish themselves prior to the first post-communist election. The early foundation of those parties allowed them to survive and to resist later encroachments on their power. All four Hungarian parties in parliament in mid-2005 have been elected to parliament in every post-communist election.

Ideological polarization destabilizes party politics by straining the consensus needed to keep the entire political system together. Polarization occurs when the ideological distance between parties at opposite ends of the party system is unusually great. It is also present when at least one important party becomes off-limits to normal inter-party cooperation (Sartori 1976:131-145). In the latter scenario, at least one party is far enough removed from the ideology of the current regime that it refuses to cooperate with parties supporting the regime, is rejected by parties supporting the regime, or is banned outright by the regime. A relatively mild case is found in the Czech Republic, where the hard-line Communist Party of Moravia and Bohemia (KSCM), the unreformed successor to the former ruling communist party, wins

significant percentages of parliamentary seats but is not compatible enough with other parties to join governing coalitions. The case is relatively mild because the KSCM has made politics more complicated (arguably contributing to a persistent difficulty in forming majority governments) but has not agitated against the democratic system in any serious way. More serious are the cases of extreme nationalist parties, primarily in Eastern Europe and the Balkans. Ethnicity has played a strong role at times in dividing parties against one another in Ukraine, Moldova, and the Baltic states. However, extreme nationalist parties have been most damaging in the former Yugoslavia. In the 1990s, the Socialist Party of Serbia and Montenegro (then still the Federal Republic of Yugoslavia) and the Croatian Democratic Union (HDZ) both used their governing powers to prosecute ethnic wars, and along the way also to marginalize or persecute political forces that disagreed with their extreme nationalist positions. Political stalemate among the three main nationalist parties of Bosnia-Herzegovina was an important cause of the Bosnian War of 1992-1995 and has risen again to hobble the fragile post-war Bosnian state. Belarus provides an example of polarization that is neither mainly communist nor mainly nationalist. Facing regular harassment and patently unfair elections, political parties opposed to the hard-line authoritarian regime of President Alyaksandr Lukashenka boycotted parliament from 2000 to 2004 and won no seats in 2004 elections widely viewed as fraudulent.

Studies of party system competition, fragmentation, and stability in Central and Eastern Europe all have contributed to our knowledge of how party systems develop in today's world. But some of the most exciting new research on post-communist party systems relates political parties either to society or to other political institutions. On

the societal end, a number of studies have examined how parties are related to social divisions, or cleavages, in an effort to better understand the electoral bases of party support (Rivera 1996, Zielinski 2002). Other generally societal studies consider how the behavior of voters and parties are connected (Kitschelt *et al* 1999, Miller and Klobucar 2000). One reason that societal studies of party politics are valuable is that they ultimately should lead to better understandings of the quality of representation that democracies can provide to their people. Studies linking post-communist parties to other political institutions have considered, for example, how parties interact with electoral systems or with particular branches of government (Moser 1998, 2001). These kinds of studies are important because they hold the promise of helping political practitioners to design more effective and responsive institutions.

### **Party Origins and Structures**

One of the most useful ways to make sense of the new multiparty systems of Central and Eastern Europe is to better understand the types of parties they contain. Parties can be grouped according to various criteria. Three of the most common ways to group Central and East European political parties are by origin, by structure, and by the ideologies and policies that parties advocate.

To group Central and East European parties by their origin is to categorize them as either historical, communist successor, or new (Wightman 1998). Historical parties are those claiming to inherit the identities, names, goals, and electoral bases of pre-communist-era parties. Prominent examples of historical parties include the Hungarian Independent Smallholders' Party, the Romanian National Liberal Party, and the Czech Social Democratic Party (CSSD). Communist successor parties, as the label implies, are



former ruling communist parties that survived into the post-communist era. Many of these parties have managed to remain important political actors, winning large shares of the vote and leading or joining governments. Some communist successor parties, such as Social Democracy of the Republic of Poland, the Hungarian Socialist Party, and the Bulgarian Socialist Party, have successfully transformed themselves into West European-style center-left social democratic parties, while others (such as the Communist Party of the Russian Federation (CPRF), the Communist Party of Belarus, and the Czech KSCM) range from partly to almost wholly unreconstructed. The third category of parties is the most diverse and numerous. Most Central and East European parties are new, and they span the entire range of ideologies and policy positions. What links them is that all were founded only at or after the very end of communist rule.

This tripartite categorization, however, has some limitations. One is simply that to group parties mainly on their origins is to rely on a characteristic that becomes less important as the transition from communist rule recedes into the past. A second limitation is that the new parties category is disproportionately large, making the overall categorization less useful. A third limitation is that it is questionable whether some parties commonly viewed as historical parties really belong in that category. Communist regimes tended to be very efficient at eliminating or severely disrupting opposition movements and networks, and did so over decades of time. That makes it harder for historical parties to claim much organizational continuity with parties of the pre-communist past, and suggests that at least some are more new than they are historical.

In the end, categorizing the parties of Central and Eastern Europe based on party origins is less useful for most analytical

purposes than categorizing based on observed patterns of actual party structure or behavior. But in one important respect categorizing by origin has proven very useful. While distinguishing parties as either historical or new tells us little about their actual behavior, distinguishing communist successor parties from others has led to valuable insights on matters such as ideological restructuring, communication with voters, coalition behavior, and party organization (Grzymala-Busse 2002, Ishiyama 2001). The communist successor category has probably proven more valuable because communist successor parties not only share origins but also share more behavioral and structural features than do the parties of either of the other categories.

A second way to categorize parties is by the organizational structures they create. In what has become a classic West European categorization, parties may be labeled as cadre, mass, or catch-all parties (Duverger 1954, Kirchheimer 1966). Cadre parties, the oldest kind, are parties whose main decisions are made by a small group of political leaders. Mass parties, which emerged with the rise of universal adult suffrage, depend for their success on the active involvement of large numbers of citizens who share key important common interests. Catch-all parties, which developed in the postwar years, are parties that widen their policy appeals to draw in a broader group of voters than mass parties traditionally target. In recent years, additional categories, such as that of the cartel party (Katz and Mair 1995), have been proposed. This kind of categorization is more complex than that based on party origin, and extensive analysis is required to use it well. But even a cursory analysis can help us to better understand an important contrast of relevance to the study of post-communist European parties. Mass parties are the most likely to build an extensive organizational structure, one that uses many local offices, clubs, and

grassroots networks to keep its electoral base involved. Cadre parties are the least likely to build an extensive organizational structure, because they are elite-led and tend to discourage active citizen involvement.

Studies of party organization in Central and Eastern Europe (Ishiyama 2001, Lewis 2003, Toole 2003) suggest that most parties in both Central and Eastern Europe have avoided developing the large party organizations characteristic of mass parties. Parties in Central Europe, for example, tend to have proportionally fewer members than traditional West European parties (Toole 2003, 104-107), while parties in Russia are generally dominated by individual politicians or by small numbers of political elites (Rose 2001). The overall Central and East European party organization pattern is most likely due in part to the fact that most parties have had little money to fund the building of large party infrastructures and in part to the fact that many citizens resist joining parties of any kind after being ruled for decades by coercive party-dominant communist regimes. Most Central and East European parties thus have organizations generally more typical of cadre parties than of the mass party type that still holds some sway in Western Europe. The main exceptions are communist successor parties, which tended to inherit much of the physical infrastructures and financial assets of their ruling party predecessors. But even they often have not been able to develop the large memberships characteristic of traditional West European mass parties.

### **Policy Advocacy**

The third and most familiar way to group parties is by the ideologies and policy positions they advocate. Political parties have the chance to implement their policies when they enter governments. But the extent to which parties—as opposed to individual politicians or organized interests, for

example—actually control the implementation of public policy is a matter of some debate (King 1969). And where parties are still developing and party systems are often unstable, as in Central and Eastern Europe, the chances that parties will strongly affect policy implementation may well be weaker than in regions where parties and party systems are well established. What parties certainly do engage in is policy advocacy.

In Central and Eastern Europe, parties compete across a wide ideological spectrum, which in traditional terms extends from the orthodox communist left to the extreme nationalist right. (While others more accurately illustrate the complexity of post-communist politics by plotting parties and policy positions across two axes rather than one (Kitschelt *et al* 1999), this summary reduces two axes to the familiar one.) Left-right labels are always difficult to generalize accurately about, and common ideological labels do not always comfortably fit into Central and East European political environments. But for its faults, this kind of party grouping can be particularly useful to non-specialists seeking to understand a region's complex party politics and policy dynamics.

The single most important feature of the left side of the Central and East European ideological spectrum is the successful regeneration of former ruling communist parties. Communist successor parties are dominant left or center-left parties in most countries of Central and Eastern Europe. As noted earlier, however, they vary in the degree to which they have moved from traditional Marxist-Leninist ideology. In general, the transformation of communist successors into genuinely West European-style social democratic parties has been most common in parts of Central Europe and the Baltics (as the cases of Poland, Hungary,

Bulgaria, and Lithuania suggest), while the maintenance of more orthodox communist ideologies has been most common among communist successors in Eastern Europe and parts of the Balkans. Other left and center-left parties exist in Central and Eastern Europe, but few have become larger than the communist successors. The Czech Republic, whose main social democratic party is not a communist successor and whose important communist successor party is unreconstructed, is a notable exception to these patterns. An interesting feature of the left side of the ideological spectrum is a decline in the coherence of Marxist-Leninist ideology among the less reformed communist successor parties. For example, a number of these parties (including the Czech KSCM, the Socialist Party of Serbia and Montenegro, the Romanian Social Democratic Party, and the Russian CPRF) have supported not only statist economic policies but also nationalist policies that communists traditionally have disavowed.

While the left side of the post-communist ideological spectrum has often been dominated by communist successors, the right side in virtually all countries contains only new or historical parties. The absence of right or center-right parties able to inherit assets, infrastructure, and social support from the communist era has left the field of competition wide open and in many countries has rendered the right side of the party system more fluid and unstable than the left side. Important parties of the mainstream right (such as the Hungarian Fidesz, Slovakia's Christian Democratic Movement and Slovak Democratic and Christian Union, and several Polish successors to Solidarity) tend to espouse secular conservative or Christian democratic policy positions but do not always use the conservative or Christian democratic labels. On the hard right are nationalist parties (such as Russia's LDP, Romania's Greater

Romania Party, and the Serbian Radical Party), which manage to gain fairly regular parliamentary representation in many countries of the region. Two features that tend to distinguish the mainstream right in Central and Eastern Europe from the mainstream right in Western Europe are anti-communism and nationalism. Anti-communism continues to inspire parties and voters across the Central and East European right, although the potency of anti-communist appeals may be waning as the communist era becomes more distant in time. Nationalism is more pervasive in Central and Eastern Europe than in Western Europe and is espoused with unusual openness even by otherwise center-right parties (Hungary's Fidesz being a notable example). While some elements of the Central and East European right are quite receptive to free-market policies, others are much less so. One interesting reason for this is the continuing appeal of nationalism, which for example has energized some parties of the Central European right to defend national economic interests against the free-market demands of EU negotiators on matters such as foreign direct investment and the foreign purchase of residential properties.

On the traditional single left-right ideological axis, centrist parties are most often liberal parties that eschew both the statist economic policies of the left and the cultural policies of the right. They tend to be fairly small in Central and Eastern Europe, as they are in most of Western Europe. Liberal parties in Central and Eastern Europe are more likely than other parties to support free-market policies, civil and political liberties, and good relations with the West. Free-market policies have been the cornerstone of two unusually powerful liberal parties, the Czech Civic Democratic Party and the Estonian Reform Party, both of which have led governments and been at least as popular as their conservative or Christian democratic

opponents. While support for good relations with the West does not distinguish liberal parties from other parties in most of Central Europe and the Baltics, it can distinguish relatively liberal parties from others in Eastern Europe (for example, in the cases of Yabloko and the Union of Rightist Forces in Russia).

As the use here of the traditional left-right axis suggests, the policy and ideological positions of Central and East European parties do bear some general similarities to those of Western Europe. But the peculiarities noted above for each of the three major sections of the axis make clear that important differences persist between Western and Central and Eastern Europe. Among the ways in which Central and Eastern Europe stand out as unique are the mix of Marxist and nationalist ideology on the hard left, the durability of anti-communism on the center-right and right, the significance of nationalism on even the center-right, and the fact that support for good relations with the West ends up being a defining characteristic of liberalism in some countries of Eastern Europe.

### **Policy Implementation**

The governments of post-communist Central and Eastern Europe have had to manage a multitude of challenges arising from their dramatic dual (political and economic) transitions from communist rule. Among the most important types of policies they have implemented along the way are economic, social, external, and ethnic ones.

The economic challenges faced by post-communist Central and East European governments have been enormous. In most countries, the state controlled all or virtually all of the legal economy, owning all businesses, farms, and shops and setting prices, wages, and production targets. (In a few countries, state control over the economy was less complete. The Yugoslav regime ran

a more mixed economy, for example, and the Polish regime failed to collectivize agriculture). Post-communist governments inherited skilled and well educated workforces, but the inefficiencies of command economies had left behind outdated technologies and deteriorating economic infrastructures. To make matters worse, important key foundations of market economies (such as stock exchanges and laws governing the buying and selling of private property) did not exist, and many states had accumulated large foreign debts. In short, the key economic challenge faced by Central and East European governments was to disengage the state from its control over the economy while preventing economic collapse and simultaneously building (often from scratch) the extensive foundations of a competitive market economy. While governments enjoyed some advantages, such as the quality of their workforces and, in some cases, their proximity to important world markets, the difficulties they faced were acute.

Of the economic policies implemented by Central and East European regimes, two kinds stand out. The first are policies designed to achieve liberalization and macroeconomic stabilization. The transition from command to market economies would only work if problems such as inflation and unemployment could be controlled enough along the way to ensure continued popular support for necessary temporary hardships. Some argued that this was best done rapidly, an approach that came to be known (mainly by its opponents) as “shock therapy” (Balcerowicz 1994). Leszek Balcerowicz, who implemented such a policy as Polish finance minister from 1989 to 1991, contended that the fastest way to achieve lasting economic growth was to take full advantage of what he termed the “period of extraordinary politics”, a short period of time right after the demise of communist rule in which ordinary people

would be willing to endure severe economic strain for the promise of better future results (Balcerowicz 1994). Among the countries that joined Poland in pursuing rapid reform were Russia, Estonia, and the Czech Republic. The opposite approach was a more gradualist one. Proponents of this method argued that popular support could only be sustained if economic strain were kept at a moderate level and if time were taken to build strong new free-market institutions before all reforms had been carried out (see Murrell 1992). Among the countries following the more gradualist path were Hungary and Romania.

The other kind of policy that stands out in Central and Eastern Europe is large-scale privatization, the transferal of large state economic assets to the private sector. Three general methods of large-scale privatization have been tried in Central and Eastern Europe. Each has advantages and disadvantages (Jeffries 2002:397-403), and governments have adopted various combinations of them (Vagliasindi & Vagliasindi 2003). One way to privatize economic concerns is to sell them directly to individuals, other companies, or groups of investors. While this has the advantage of bringing revenue to the state from investors able to pay, the disadvantage is that during the early transition years few Central and East Europeans could afford to become investors. That meant that governments choosing this option often had to sell off many assets to foreign investors (and in so doing risk a backlash from voters). A second method is mass privatization, in which shares in state assets are distributed evenly throughout a country's population. This method has the advantage of keeping ownership of a country's economic assets in domestic hands (and thereby keeping the popularity of privatization high), but it has the disadvantage of raising virtually no revenue for state use. The third method is the management-

employee buyout, in which ownership is transferred to those already working for the state-owned companies concerned. This method shares with mass privatization the advantage of keeping assets in domestic hands, but one of its key disadvantages is that it can lead to corruption and to the concentration of economic power in the hands of former communist elites. Central and East European governments usually favored one approach but also used at least one other approach as well (for a comprehensive country-by-country summary, see Vagliasindi & Vagliasindi 2003, table 3.2). Countries that primarily chose direct sales include Poland, Hungary, and Estonia; countries that primarily used mass privatization include the Czech Republic, Latvia, Lithuania, and Armenia; countries that primarily used management-employee buyouts include Romania, Slovakia, Albania, Russia, and Ukraine. There is some regional variation in the primary methods chosen. Only Central European and Baltic states used direct sales as their primary method, while all but one country to primarily use mass privatization were East European. Primary users of management-employee buyouts included a mix of countries from both Central and Eastern Europe.

By the end of the first post-communist decade, economic performance had begun to vary dramatically across the regions of Central and Eastern Europe. While all countries first experienced considerable economic contraction and only later rebounded, the contractions were deepest and most prolonged in the former Soviet economies and most shallow and short-lived in Central Europe. On average, Central European economies bottomed out in 1993 after contracting by roughly a fifth and then rebounded to 1989 GDP levels in about 2000. The Baltic states on average bottomed out in 1994 after contracting by almost half and then

rebounded to three-quarters of 1989 GDP by 2001. The former Soviet states (including the Baltic and non-European states) reached their average low in 1998 after also contracting by almost half and rebounded by 2001 only to 65 percent of 1989 GDP. There are exceptions—with Serbia and Montenegro and Moldova far below the others in their regions and Estonia considerably above the Baltic average—but the regional differences hold up remarkably well when individual country results are compared to one another.

The most important social policies implemented by Central and East European governments concern the welfare state. While the transition to a market economy could be expected to increase living standards over the medium to long term, the costs over at least the first decade of post-communist history were high. The transition created many social problems, such as unemployment and homelessness, that had been unknown or effectively hidden under communist rule (Andorka *et al* 1999). While post-communist states did begin to shift to more market-oriented methods of social policy, the pressures to maintain welfare states at levels comparable to those seen in Western Europe were considerable. Voters expected no less, and the EU demanded certain minimum welfare state standards before countries would be accepted for entry. The net result was that welfare states tended not to contract dramatically, even if the methods used to implement specific social policies did change in important ways (Manning 1995, Elster, Offe and Preuss 1998:ch 6).

External policies have been particularly important in post-communist Central and Eastern Europe, as countries have rearranged foreign policies that had unified them during the Cold War years. For Central Europe and the Baltic states, the foremost foreign policy goals have been accession to the North Atlantic Treaty Organization (NATO) and the

EU (Solomon 1998, Henderson 1999). EU accession has generally been the primary goal, as it is viewed by elites and most citizens alike as a ticket to economic prosperity. NATO accession, however, has been the easier first step, used as least as much as evidence of progress toward EU membership as to enhance security. By 2004, NATO had enlarged to include ten Central European and Baltic states (Bulgaria, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia, and Slovenia). The road to EU membership naturally is more difficult than the road to NATO membership, given that the EU—by far the world's most advanced experiment in economic and political integration—is a much more comprehensive organization. After years of negotiation, eight Central European and Baltic states (all the post-communist NATO members except Romania and Bulgaria) won EU membership in May 2004. Romania and Bulgaria are slated to join at about 2007, with Croatia the most likely next new member at least several years later. EU accession is neither as likely nor as popular in non-Baltic Eastern Europe. Russia has strongly opposed encroachment by both NATO and the EU on former Soviet territory (though it failed in the end to deter the Baltic memberships in both organizations) and likely will continue to work hard to limit further eastward enlargements to the old western border of the USSR. Most of the East European states are far from meeting the requisite EU accession qualifications anyway, although democratic revolutions in Georgia (2003) and particularly Ukraine (2004) increased talk of those countries' accession prospects.

For states harboring EU ambitions, the drive for EU membership dramatically transforms virtually all areas of state policymaking. Earning accession means convincing EU institutions and all EU

member governments that one's political system is fully democratic and that one's economy is a fully functioning market economy. It also means adopting the full body of EU law, known as the *acquis communautaire*, into national law before joining. The *acquis* addresses virtually all imaginable features of economic policy (and many features of other policy) in minute detail and runs upward of 60,000 pages. In some ways, the need to implement the *acquis* has proven useful, as it has provided post-communist governments with ready-made wording to laws that needed to be written or rewritten anyway in the course of establishing modern market economies. But implementing the *acquis* has also absorbed years of legislative effort in the parliaments of post-communist Europe. Even states that remain far from qualifying often find it best to implement as much of the *acquis* as possible, both to keep them on the road to possible accession and to make their economies more competitive with those of the rest of Europe.

But EU and NATO accession are not the only important external policy issues. Russia, as the only large power among Central and East European states, has had to struggle with its decline in global dominance (Bowker 1997, Kuchins 2002). It still carries weight as a veto-wielding member of the UN Security Council and remains actively involved in regional crises around the world. It joined the G-7 (then renamed the G-8) in 1998, though some questioned whether its membership was deserved. After the September 2001 terrorist attacks Russia became an enthusiastic supporter of the US-led war on terror, but it later balked at supporting the US-led war on Iraq. The security of Russian nuclear weapons and technology has been an important policy issue throughout the post-communist years, particularly as concerns over nuclear proliferation have grown. Belarus and Ukraine, the only other Central or East

European states to hold nuclear weapons, have given up their shares of the former Soviet stockpile.

Ethnic policies, those promoting the interests of one ethnically defined nation over others, have proliferated in post-communist Central and Eastern Europe since 1989 (Burg 1996, Fowkes 2002). While some have produced only political tensions, others have led to brutal wars. In former Yugoslavia, the central state (which increasingly represented Serbs rather than breakaway Croats, Bosnian Muslims, or Slovenes) and the new Croatian state effectively prosecuted ethnic wars against one another and against Muslims in Bosnia from 1991 to 1995 (Silber and Little 1995, Burg and Shoup 1999). The rump Yugoslav state later intensified already harsh longstanding policies targeted at Albanians living in its Kosovo region, provoking a 1999 war with NATO that cost Yugoslavia its control over Kosovo. The extreme ethnic policies used during the Yugoslav wars have been well documented, and included the use of concentration camps, mass slaughter, systematic rape, and ethnic cleansing (Rohde 1998). In 1993 the International Criminal Tribunal for the former Yugoslavia (ICTY) was established in the Hague to try individuals for crimes against humanity committed during the wars. In southern Russia and the Caucasus, states have clashed with ethnic separatist groups in sometimes brutal conflicts that remain unsettled as of 2005. Russia has fought brutal wars against separatists in Chechnya (Evangelista 2002) and has directly or indirectly supported breakaway movements in the Transdniestr region of Moldova and in the Georgian regions of South Ossetia and Abkhazia. Conflict in and around Nagorno-Karabakh, a mainly ethnic Armenian enclave within Azerbaijan, continues to hamper relations between Armenia and Azerbaijan.

Other ethnic policies have contributed to ethnic tensions but have not led to war. Attempts at managing ethnic disagreements failed in Czechoslovakia, which divided peacefully in January 2003 into independent Czech and Slovak states. In Estonia and Latvia, governments have imposed policies limiting the citizenship and language rights of ethnic Russians, drawing ire from Russia and disapproval from pan-European institutions. The nearly three million ethnic Hungarians living in Romania, Slovakia, Ukraine, and several former Yugoslav republics have been the subject of competing ethnic policies throughout the post-communist era. Romanian and Slovak governments imposed discriminatory policies on ethnic Hungarians in the 1990s, while relatively aggressive Hungarian policies (which have gone so far as to offer Hungarian state benefits to co-ethnics abroad) have been viewed in turn as intrusive by Hungary's neighbors. Tensions also persist elsewhere, for example between ethnic Bulgarians and ethnic Turks in Bulgaria, between ethnic Ukrainians and ethnic Russians in Ukraine, and between ethnic Russians and other ethnic groups in parts of Russia. And throughout post-communist Europe, states have discriminated against the Roma, formerly known as Gypsies (Guy 2001). In many of these peaceful cases of ethnic tension, pressure by international organizations has led to a moderation of discriminatory practices. EU pressure has been especially effective, since the EU demands that ethnic policies conform to its standards before membership in the Union can be granted.

## **Conclusion**

The transition from monopolistic communist rule to pluralistic (if not always democratic) politics in Central and Eastern Europe has profoundly influenced both political parties and public policies. The region's newly

multiparty systems have become far more competitive, even in countries that remain undemocratic. But levels of real competition vary, and the party systems of virtually all countries continue to be less stable than those of Western Europe tend to be. The ideologies and policies advocated by Central and East European political parties can be classified in part using familiar left-right labels, but the region's unique history also causes them to diverge in important ways from the familiar classification. Post-communist governments in Central and Eastern Europe have faced severe political, economic, and social problems and have had to devise new public policies to try to deal with them. Among the new economic policies have been those devoted to liberalization and macroeconomic stabilization and to the privatization of large-scale enterprises. Governments also have created important new policies aimed at reforming welfare states, at changing relationships with the outside world (often in pursuit of NATO and EU membership), and at managing or exacerbating ethnic tensions. Patterns of party politics and policy implementation vary across the twenty-two countries of Central and Eastern Europe, with Central European and Baltic states the most likely to approach West European norms. At the same time, their shared communist past continues to distinguish all Central and East European states in significant ways from states to the west of the old Iron Curtain.

Whatever the future holds, it is unlikely to burden the countries of the region with a return to old-style communist rule. Politics in contemporary Central and Eastern Europe is a mix of old and new, of communist legacies and other forces. In many countries, the fact or promise of EU membership is likely to continue to move politics and government more toward West European patterns. And even where communist legacies remain more entrenched, those legacies become



increasingly corrupted—for better and worse—by other international and domestic influences. Nationalism, liberal political ideals, and free market forces all conspire to transform even the region's most stolid dictatorships into regimes that only partly resemble their communist forebears. Shaped by various combinations of communist and post-communist influences, the parties and policies of Central and Eastern Europe continue to evolve in unique ways. They promise to remain valuable objects of scholarly interest for some time to come.

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Europa. [europa.eu.int](http://europa.eu.int)

European Bank for Reconstruction and Development. [www.ebrd.com](http://www.ebrd.com)

Organisation for Security and Cooperation in Europe. [www.osce.org](http://www.osce.org)

Radio Free Europe—Radio Liberty. [www.rferl.org](http://www.rferl.org)

Transitions Online. [www.tol.cz](http://www.tol.cz)

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## Economic Planning

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### **Introduction**

Economic planning is the process of direction and control of national economic activity by an administered board appointed by the government, usually referred to in the literature as the central planning board (CPB). Economic planning provides for conscious social direction of economic activity, mainly investment in achieving a socially beneficial outcome. Economic planning is contrasted against free markets. As the amount of investment directly determines the level of economic growth, employment and living standards, investment cannot be left to the capricious free market forces. It is argued that if investment is left to market forces alone the free market will be self-destructive, fostering income and wealth inequalities and the lack of opportunities. Alternatively, economic planning through mainly the public regulation of investment will ensure the achievement of full employment and stimulate economic growth in line with the social benefit.

In this entry we address national economic planning, in other words the planning of the whole economy. This is in contrast to partial or specific economic planning, i.e. planning for a particular part of the economy. Partial planning for example might take the form of industry policy (designed to assist enterprises in confronting competitive forces through the provision of information, tax concessions and tariff protection). Then again, partial planning might take the form of incomes policy (central administration of wages and incomes or under a tax-based incomes policy, firms that pay a wage increase above the socially acceptable non-inflationary level, based upon the average labor productivity growth, are penalized by higher taxes). As expected, such partial allocative plans suffer from their

partial character which ignores interdependencies between sectors.

Supporters and opponents of economic planning set forth a number of different arguments. Supporters argue that planning provides practical measures to ensure the production of essential goods without relying on the instability associated with free markets. The government can exploit resources to achieve social objectives decided through a democratic process. Individualism can be controlled in favor of greater capital investment in economic development in a societal-desired pattern. For example, the state can begin building an industrial base rapidly in an underdeveloped economy without waiting years even decades for capital to accumulate through the expansion of light industry, and without reliance on external financing. Economic planning can maximize the utilization of all available resources, while also avoiding business cycles. Based on the economic plan, neither unemployment nor idle production facilities should exist and the economy should grow in a stable pattern, avoiding inflation and recession. An economy based on economic planning can achieve social rather than individual goals. Economic planning eliminates the dependence of production on individual profit motives, which do not necessarily provide for all society's needs. Economic planning enables authorities to concentrate resources according to society's priorities without being affected by considerations of profitability, private capital interests and individualism.

Critics of economic planning on the other hand argue that planners cannot determine demand with sufficient precision, as markets do. Shortages are common in a planned economy, for example consumers will queue to buy even basic goods. These shortages are due in part to the CPB deciding, for instance, that producing weapons is more important

than producing bread, or because commands were not given to supply the bread factory with the right amount of wheat, or because the CPB had not given the bread factories the incentive to produce the required quantity and/or quality of bread. Even the market socialist Nove (1984:37) admits that “the function of prices do indeed include vitally important transmission of information. The price mechanism is a ‘must’”.

Supporters of free markets believe that an economy achieves efficiency when there is as little government intervention as possible. In contrast, economic planning requires a state which intervenes and distorts individual decisions and market outcomes. Friedman (1984:10) states “the real beauty, and the use of the word ‘beauty’ advisedly, of a price system is precisely the way in which the incentive to act on information accompanies the information that is transmitted. This is not true in a command economy. Information is transmitted from one level of a command economy to another, but that information does not carry with it any incentive to act in accordance with it. There must be some kind of supplementary means of seeing to it that people act on the information”. Anyway, government economic policy is ineffective, at least in the long run.

### **Types of Economic Planning**

There are different types of economic planning. These types vary based on goal that planning attempts to achieve and the structure of the economy. Economic planning can take the form of central planning in a command economy (centrally-administered socialism) by the use of direct controls such as the Stalinist economies of the Soviet Union, Eastern Europe and China. Central planning is the operation of a command economy through centralized decision-taking. In such an economy, decisions are made at the centre and orders are issued to enterprises

concerning their production and investment plans. Central planning was attempted in the former Soviet Union, Eastern Europe and China. Experience demonstrates that central planning was so inefficient in these countries that they abandoned central planning and have adopted market relations and increased the role of markets in the economy.

Nonetheless, economic planning is not only a feature of “socialism” as practiced in the aforementioned countries. It also became an important part of regulation of economic activity in economies that did not adopt “socialism”, that is in market based capitalist economic systems. Economic planning in capitalist economic systems came into existence in many capitalist nations after WWI and WWII in an effort to assist in the reconstruction process. Most commonly, planning in capitalist economic systems has taken the form of indicative planning which is basically planning based on the distribution of information, indirect controls and market instruments. The limited economic success of economic planning under capitalism and the final collapse of centrally-administered socialism has stimulated a passionate debate about the benefits of economic planning. Presently, most capitalist economies dismiss economic planning. The most common form of planning in today’s capitalist economies takes the form of partial economic planning as industry policy and/or incomes policy.

For most Marxists the experience of Stalinism and of capitalist market planning resulted in the adoption of a “pragmatic” approach to socialism, in the form of market socialism. Market socialism is concerned with the optimal combination of centralization and decentralization, markets and planning, individualism and the common good, and public and private property. This is because, as Nove (1984:40) states “markets clear only on far-fetched assumptions not satisfied in the real world. A market economy may be a

necessary condition for human freedom, but it is certainly not a sufficient condition. In many countries its maintenance seems to require military dictatorships or even death squads. A free market provides some irreplaceable advantages, but does not solve all the problems. State intervention can and sometimes does have negative consequences, but universal deregulation is no panacea". While there is no actual experience of market socialism, supporters of this economic system argue that it achieves the right balance between markets and economic planning in the form of market planning.

### **Economic Planning in Practice**

#### ***Central Planning in Command Economies***

In the "socialist" economies of the ex-Soviet Union, Central and Eastern Europe, Asia and Cuba coordination of economic units was, and in some of these countries still is, based on central planning. The economic system in this case is named centrally administered socialism or Stalinism. The Soviet system of central planning, adopted later in other countries, was developed during the 1930s after the adoption of the First Five Year Plan in 1929. It was facilitated rapid economic growth, maintained full employment and low rates of inflation, and was associated with an increase in living standards and cultural development. It coexisted with repression and violation of individual freedom, arbitrary decision-making, inefficiency and waste, wide-spread pollution and environmental degradation, endemic shortage, and lack of consumer satisfaction.

Stalin interpreted Marx's writing as requesting that the "socialist" economy be structured on a command basis. With respect to property relations, under the Stalinist system all non-labor means of production were non-privately owned. Virtually all capital, land and natural resources were state-owned. Collective property was allowed in

the form of collective farms and some retail outlets. The Stalinist economic system has also been described as a "command economy". This is because the model relies upon a centrally administered or bureaucratic form of organization with the market largely replaced by a set of commands or directives issued to the enterprises by the central administration. Such commands were set in such a way as to achieve balance, (i.e. quantity supplied equals quantity demanded), and the allocation of resources, was based on what was desired by the central planners. This model is associated with a development strategy of extensive growth. Extensive growth strategy emphasizes the expansion of production primarily with the use of additional resources, capital investment and/or increasing the labor force. Extensive growth provided the means for rapid industrialization which, Stalin stressed, was necessary for the survival of socialism.

The policy decisions took the form of five-year plans, which set targets in both physical and monetary terms. The central targets were then disaggregated and, through the state apparatus, reach each enterprise in the form of specific directives concerning the level of gross output, the increase in labor productivity, and the amount paid in wages, where and when the output must be delivered, etc. The recipient of the targets was the enterprise manager, who was a salaried employee and assumed full responsibility for the implementation of the enterprise's plan. The enterprise was run on the basis of "one-man management". The managerial system was authoritarian in that the central authorities appointed the manager – a male – and he was not accountable to his own workforce. Most of the time, there was no direct worker participation or trade union participation in running the enterprise. The manager's responsibility was to fulfill the plans at any cost. To ensure that the centrally

determined targets were met, a system of penalties and rewards was used, depending on whether targets were over-fulfilled, fulfilled or under-fulfilled. Thus, the enterprise manager operating in the command economy found the most important constraints on his decision-making power were non-market constraints. These non-market constraints ensured that enterprise managers had little effective decision-making power, as the major task of the manager was to achieve the targets of the central plans which were determined by the central authorities. Hence enterprise managers in a centrally administered system, in contrast to their counterparts in the market system, played an insignificant role in the determination of enterprise objectives.

Meanwhile, consumers were able to choose from whatever goods and services were available. It should be pointed out that the composition of final output was determined collectively by the communist party and the state. There was consumer choice but no consumer sovereignty. Thus, Stalin broke the unity between consumer choice and sovereignty. The breakdown between consumer choice and sovereignty in the Stalinist model reflects the non-pluralistic character of the economic structure. Preferences were largely determined by the communist party. The state planners had to draw up plans, which were consistent with the party preference function. Prices were centrally determined and were often set below the market-clearing level, with queues used to ration deficient supply.

A rejection of the market mechanism in production, as in the case of the Stalinist model, places the burden of a non-wasteful allocation of resources on the CPB. This is an enormously complex task. Since the central authorities required a vast amount of accurate information, which is difficult to obtain, and due to the inability to solve the computation

question. An important contradiction stems from the simple fact that the center cannot know in full detail what was needed by the society, and yet the entire logic of the Stalinist system rested upon the proposition that it is the duty of all subordinate management to obey instructions from the center. This is because they supposedly embody the needs of the society. This is the result of the non-pluralistic nature of the economic structure. Even if it were possible for a centrally administered form of organization to provide adequate information, it would take a considerable period of time to adjust to the continually changing conditions associated with the dynamic process of economic development and growth. Thus, central administration lacks the flexibility of market relations.

A further source of waste stems from the presence of conflicting incentives, information asymmetry, and the principal-agent problem. In particular, the existence of conflicting objectives between the central authorities and the enterprises results in inconsistent actions. Managers demand the greatest possible volume of investments, quantities of labor, material and machinery and easy targets. They were interested in maintaining a routine, a quiet life, avoiding changes. There was an incentive to hoard materials in order to ensure that future output targets could be met, given the unreliability of supplies. If the supplies dry up, the managers depended on the "tolkachi" (pusher), which were essentially middle men with special connections, who were able to cut through the bureaucracy and arrange by any means, almost invariably illegal, the needed supplies. Managers tended to mislead or even falsify data relating to the performance of the enterprise. They understated their potentialities and overstated their needs. This had disastrous consequences for the economy, which lost one of the important means of



functioning accurately, which is the objective information about needs, reserves and potentialities.

Managers tried to make plan fulfillment as easy as possible. They had an interest in narrowing down the range of goods produced and avoiding the production of new products and innovations. They preferred to produce goods that used large quantities of material at the expense of quality. On the other hand, the central authorities tried to reduce and limit the demands for investments, for human labor power and materials, and to push for higher targets. Because the central planning body knew the likely behavior pattern of management, the planners tended to proceed on the basis of past reported performance. This, in turn, led cautious managers to avoid “excessive” improvements in performance, which would cause them to be given greater tasks in the next plan period. In the end a compromised subjective command emerged, which was in the interests of both parties, but probably not in the interest of the economy.

There can be no doubt that the Stalinist system, in spite of its shortcomings, worked for some time as a vehicle of rapid economic growth, particularly in industry. The achievements of the non-pluralistic system were noted around the world between the 1930s and early 1950s. While the system was inappropriate for achieving even modest increases in labor productivity in the long run, a rapid increase in material production was possible as long as the sources of extensive growth existed. Once they were exhausted, the rate of growth of material production inevitably declined and since immaterial production was always discounted, inconsistencies developed. Thus, economic growth in the Stalinist model was based on the successful utilization of the sources of extensive growth. Without this, a high rate of growth of material production is not possible. The elimination of the sources of extensive

growth and the development of inconsistencies inevitably resulted in the collapse of Stalinism since the system lacked internal forces making possible the shift from extensive to intensive growth.

### *Indicative Planning in Capitalist Economies*

Economic planning under capitalism is usually the result of disruptive political and economic situations arising from wars or economic depressions. As Gruchy (1984:177) notes “it is crises that move nations to action”. After WWII there was a widespread adoption of planning programs by various capitalist countries in Western Europe under pressure from the demanding circumstances of the early postwar reconstruction.

In a capitalist economic system through the usage of a plan, the state seeks to influence individual choices rather than to make choice collectively: the plan takes the form of a statement of intent. The statement of intent is an “indicative plan”. Pure indicative planning occurs when the targets of the plan are purely voluntary in character, involving only information provision but no financial incentives or coercion. In reality, the planning experience of capitalist economies was never purely indicative (Estrin and Holmes 1990:532). Indicative planning enjoyed great popularity in the 1960s, but thereafter it fell out of favor as part of the general increase of faith in, and reliance on, market outcomes. The change in direction of economic theory towards future markets, optimal contracts and rational expectations reduced the demand for indicative planning. The dominant perception of economic theory today argues that markets more or less function efficiently, that agents are able to make reasonable forecasts of the future, and that government efforts to gather information from agents and/or to influence economic outcomes are likely to be ineffective (Brada and Estrin 1990:525). Though it is now one



of the instruments least in favor with Western neoliberal administrations, some of the most successful economies of the 1980s, including Japan and Sweden, still plan.

Indicative planning was instituted as a response to the failures of the market system in attaining socially desirable objectives. It is distinguished from other policy instruments that deal with market failures in that it focuses on market failures that result in the nature or availability of information influencing long-term outcomes. For this reason, indicative plans have the important element of information pooling and provision. At the same time, the feature that distinguishes indicative plans from plans in command economies is that neither firms nor consumers nor labor unions are formally obligated to fulfill the objectives of the plan. Indeed, the government itself is often not obligated in any formal way to achieve plan targets and in reality may place relatively little emphasis to achieving its plan objectives. If the authorities actually do seek to implement the plan, they must rely on indirect government tools such as taxes and subsidies.

The idea was first conceptualized by the economist and French Planning Commissioner Masse (1962) and formalized by Meade (1970). Masse argued that the formulation of a common view of the future on which people acted could substitute for the absence of future markets. Meade showed that, in principle, exchange of information via indicative planning could exactly duplicate the Arrow-Debreu equilibrium. This could, as Meade pointed out, remove the endogenous or market component of uncertainty. Any remaining uncertainty could be covered by insurance or born by the participants of the transaction. The welfare-enhancing properties of such indicative planning would result by either moving the economy to a new equilibrium associated with lower risk costs

or moving the economy from disequilibrium into equilibrium (Estrin and Holmes 1990:533).

Information gathering and processing are characterized by economies of scale, which necessitates a role for the government in the form of an indicative plan in the field of information collection. There is certain cost in the process of collecting information arising from the fact that this process requires an early large investment in capital and labor-power. After this heavy initial investment has been made, the additional cost of gathering and processing new information is substantially reduced. Furthermore, associated with these economies of scale are the externalities created when economic information collected by the government is treated as a public good available to all decision-makers. These externalities arise because private interests do not coordinate their information gathering and processing, while the government is in the best position to collect and provide information to private decision-makers about alternative investment paths that they may have been overlooked. Indeed, the information available in the plan might well be viewed as a public good (Miller 1979). Treating information gathering and processing as a public good can in this manner contribute to a use of the economy's scarce resources in the most socially desirable way (Gruchy 1984:174). In addition, the planning process would also help reveal real externalities associated with major planned investment projects. Thus, adjustments could be made prior to the initiation of the projects; action is preferable to *ex post* correction. Finally, potential immobilities of resources and the need of restructuring the economy can be identified and action taken in advance to reduce the significance of this inefficiency.

Some countries, like Japan, rely primarily upon a type of economic planning that supplies information to private businesses

which is gathered and processed collectively and also provides government financial assistance to large-scale investment in order to achieve high and sustained levels of production and employment. Japanese economic planning emphasizes achieving national goals of high and sustained levels of production and employment with the aid of collective or state gathering and processing of economic information. Also, financial aid to both high technology and old industries, and a minimum application of mandatory economic and financial controls to private business. The success of Japanese planning, with its heavy reliance on voluntary collaboration among government business, banking, and labor, is based largely on the presence in Japan of a national consensus that economic problems should be met in a voluntary and cooperative manner. Importantly, there are certain cultural and historical circumstances in Japan that favor the emergence of a work ethic and a concern for high quality effort in work (Gruchy 1984:169-70). Economies such as France, Norway, and Sweden utilized national plans that provide much closer governmental supervision of private economic and financial activities than Japan (Gruchy 1984:68).

Although the Norwegians have been planning since the 1930s and the French, Japanese, Swedes and Dutch since just after WWII, one of the striking features of the literature is the absence of any consensus on how successful such planning has been. Early evaluations of planning were highly positive. This was probably because the planners were given sole credit for the excellent growth performance of the French and Japanese economies between the late 1940s and 1960s. The assessment changed when planning provided neither the French nor the Japanese with any particular advantage in dealing with the recession which followed the oil crash in 1974. This negative perception was

reinforced by the publication of a number of studies that were more skeptical about the success of indicative planning. Moreover, the negative assessment of indicative planning was consistent with the change in economic policy direction in the 1980s that was hostile to state intervention in the economy (Estrin & Holmes 1990:538-9). A study regarding indicative planning in France concluded that in the early plans (1952-57 and 1957-61) the planners did indeed predict outcomes better than private alternatives but the reverse was true for all the later plans, and in particular for the Vth (1965-70) and the VIIth (1975-80) plans (Estrin and Holmes 1983:ch 3;1990:540).

Achieving flexibility without undermining the confidence of enterprises in the stated targets represents a major challenge for planners. Failure to successfully meet this challenge is likely to result in even greater uncertainty than that which would have occurred in the absence of a plan (Ward and Kulkarni, 1987, p.44). The unsatisfactory experience with the National Economic Development Corporation in Britain in the early 1960s and the breakdown of economic planning in France during the 1970s demonstrates this concern. While actual planning exercises in developed economics have typically contained both a micro-informational and a macro-policy dimension, the latter has increased since the 1960s. For example, French plans ceased to have detailed industrial forecasts after 1970, and indeed after 1975 they contained virtually no numerical forecasts at all as part of the plan proper, as distinct from technical appendices (Estrin and Holmes 1990:535). The deterioration in French planning stemmed from the collapse of forecasting credibility following the Vth Plan, when the planners incorrectly forecast slower growth and less inflation than actually occurred or would have

been sensible to predict on the basis of previous trends (Estrin & Holmes 1990:536).

The critics of indicative planning argue that the growing complexity, and the resulting greater interdependencies within capitalist economies make it unrealistic to expect that planners can accurately forecast aggregates for five years ahead, let alone derive meaningful as well as consistent disaggregate targets (Ward & Kulkarni 1987:45). In addition critics do not accept the claim that indicative planning will improve economic efficiency by harmonizing agents' expectations about the future. The case for indicative planning can only be made on the basis of some government advantage in gathering and processing economic information. Such advantage might exist, as already argued, due to economies of scale and asymmetrical information. However, it is not clear that the private provision of the information available in the plan results in an optimal supply of such information since the utilization of such information provides externalities to other agents (Brada & Estrin 1990:527-8). Moreover, the conflicts between planners and officials charged with monetary and fiscal policy in France suggest that the mere construction of indicative plans is no guarantee that government policies will be coordinated. The experience of other countries confirms the existence of conflicts between policy makers with a short-term goals and planners with a long-term orientation (Brada & Estrin 1990:528).

Market failures associated with information processing may have become less serious in developed and developing economies since the first indicative plans in the 1940s. Cheap computing technology and the plethora of private information sources available in the 1980s may have reduced the economies of scale in information. One of the great successes of French planning between the 1940s and the 1960s was the ability,

looking at the economy as a whole, to predict the effect of changes in macroeconomic parameters which individual firms could not easily forecast for themselves on the basis of projecting past experience. However, where the source of the uncertainty is exogenous to the economy, information pooling by itself cannot directly reduce the uncertainty, but at best only improve knowledge. As Meade noted, indicative planning is really geared toward market uncertainty. In practice, external uncertainty regarding new technological developments or the world macro-economy appears to have become more important in recent years, with faster technical change and greater international interdependence (Estrin & Holmes 1990:534) substantially reducing the effectiveness of indicative planning.

### ***Market Planning in Socialist Economies***

Most central planning was implemented by countries that referred to themselves as socialist. Nevertheless, a centrally planned economy should not be seen as the only form of socialism. Considerable amounts of planning in the economy supervised by government can be possible within the context of a market economy where the means of production are socially owned. Anti-socialists have used the criticisms of the command economy as a means of objecting to socialism. However, many socialists have pointed out that socialism can occur in a context of a market economy and not just a command economy and the collapse of Stalinism is not an indication of the infeasibility of socialism. As Nove (1984:31) stated "the attempt to eliminate the market, which Marx and Engels thought would be a simple matter, has proved to be either impracticable or highly inefficient of both at once". However, the exact definition of "socialism" is hotly disputed and therefore the relationship between economic planning

and socialism depends on the type of socialism in question.

The historical antithesis between plan and markets has been largely abandoned and some form of market socialism has emerged as the principal economic model advocated by socialists. In this entry we will be concerned with what Yunker (2001:1-34) names “pragmatic” socialism in the form of market socialism. Market socialism, as the name implies, is a combination of a market system and socialist principles. Market socialism is distinct from other economic systems due to its different goals that the system wants to achieve: prevent exploitation, reduce alienation, provide greater equality of income, wealth, status and power, and the satisfaction of basic needs. Dobb (1955,1960) in particular, argued that economic planning is desirable precisely because it enables outcomes that differ from those produced by the operation of market forces. From this perspective, the essence of economic planning is that it makes possible the coordination of interdependent decisions before they are implemented. It substitutes the conscious planned coordination of decision *ex ante* for the market mechanism’s unplanned *ex post* coordination as atomistic decision-makers respond to changing market prices and profit opportunities. Dobb (1955, 1960) also suggested that if government controlled consumption and production decisions, there would be no issue of “inefficiency” in a socialist economy.

Interdependence in economic activity is more pronounced in relation to major investments. Dobb (1955,1960) stressed the significance for planning is the distinction between unavoidable uncertainty that arises from the necessary lack of knowledge on the part of atomized decision-makers and their rivals’ intended actions. Investment decisions in capitalist economies are made on the basis of expectations about future profitability.

Future profitability depends in part on the combined effect of all simultaneously undertaken projects. However, in fragmented, atomistic, market-based decision making, individual investment decisions are made in ignorance of the actions of others. Hence, the expectations underlying investment will generally not be realized. Economic planning enables this interdependence to be taken into account. In a market planned economy, major investments bringing about non-marginal changes can be planned together and coordinated before resources are committed. As Nove (1984:31) explains “the degree and nature of the uncertainty which faces a would-be investor today are on a scale which renders correct or rational decisions less than probable”.

In contrast to capitalism, market socialism, in which the means of production are socially owned, provides conscious social direction by combining markets with planning in a way that makes the best use of both instruments (Elson 1988:310; Miller & Estrin 1994:246). In market socialism, the sectoral and spatial distribution of investment would be subject to both political as well as economic pluralism. The national five-year plan would have been based primarily on the plans of the enterprises, which themselves were derived from projected market demand. In addition to taking into account the interdependence associated with investment decisions, the planning process would have been a process of debate. Even the greatest precision in the economic calculus will never eliminate the necessity for making political decisions in drawing up plans of development. “No neutral decision rule is at hand because the contending claims are usually non-zero-sum” (Maier 1991:56). It follows that the optimization of economic decisions embodied not only the system and techniques of economic calculus but also a corresponding political mechanism within which conflicting

interests could have been clarified and compromised upon. The democratic process itself could have helped educate voters as to the real alternatives they faced and engaged their cooperation rather than their resistance to needed measures (Roemer 1992:268; Weisskopf 1993:131). All would have participated in the decision-making, so that the decisions made, in the name of society, were as close as possible to real social preferences.

Plans would be approved by an elected parliament and implemented within market relations mediated by the discretionary power of the state. For the regulation and application of plans, political pluralism (effective participation of the people) and economic pluralism (market relations) were necessary. A market socialist economy involved a continuing role for the state, one that was much subtler, more indirect and more benign than running an administrated socialist economy (Weisskopf 1996:283). In contrast to the central plans under Stalinism, reliance would have been primarily on market instruments. The plan is characterized by flexibility. Additionally, democracy makes the state's task more difficult, since a variety of inconsistent objectives will be reflected in the preferences of individuals, groups of citizens, and political parties (Belkin 1994a:32). Trade unions would have an important role as well. They would be more active in participating in the social sections of the plans and in setting forth their own alternative proposals. Thus market socialism was not a regime of technocrats, but a form of economic management that left ample room for pluralism and democratic processes of decision-making (Barratt-Brown 1995:239).

The plan will determine priorities. It will reflect the priorities of society as a whole and those of separate social groups whose interests are recognized as being especially important. Prioritizing is a complex process

and has to be based on social compromise within an open and pluralistic-democratic system. Social and investment priorities were inevitably political decisions for instrumental and desirable reasons (Roemer 1994a:299). Planning is a decentralized and democratic process of consultation and discussion, concerned exclusively with plan construction and elaboration. The process provides a forum in which information can be pooled. Also, diverse interest groups can confront one another about spillover effects, giving voters an equal voice in determining the plan's objectives (Belkin 1994b:162; Estrin & Winter 1990:123; Howe 1994:68). In itself, the plan does not contain an implementation procedure. As every actor 'bargains' through the process of negotiated co-ordination, rather than price taking, a social desirable outcome would occur. "Such a procedure contains rather more teeth than might at first sight appear" (Estrin & Winter 1990:116) because one of the major actors in a market socialist economy is the state (Roemer 1991:563). However, the use of the political process to decide investment planning "opens up the Pandora's box of rent seeking, the wasteful use of resources by interest groups who aim to influence the outcome of the process" (Roemer 1994b:106). Yet, under socialism, the tension between sectional and social interest is explicit, with the possibility of partial reconciliation and also some transformation of the perceptions and levels of social awareness of those involved. Moreover, nobody is able to impose their preferences as a result of unequal power.

## **Conclusion**

Summing up the negative characteristics of central planning of the Stalinist non-pluralistic system of economic development, we observe the following: rapid industrialization, which was promoted at the expense of the development of other

productive sectors of the economy, especially agriculture and services; inefficiency in all branches of production; failure to modernize production technology; and relatively high consumption of raw materials. In addition, when the sources of extensive growth were exhausted a shortage of labor appeared and consequently there was a slow down in the rate of material production. Given the absence of a variety of consumer goods and lack moral incentives, the incentive system broke down. Terror became the natural alternative for the central authority to be able to enforce its decisions. Hence, it appears that the Stalinist economic structure did not facilitate, but rather inhibited, the shift from extensive to intensive growth, which ultimately resulted in the collapse of the economic system.

The theoretical rationale for indicative planning is that uncertainty is a key aspect of the real economic world and is accompanied by two basic problems. One is the imperfect information that individual agents use in making decisions involving production, pricing, investment, and other economic matters. The other problem relates to the technological changes that have affected the structure and functioning of the advanced industrial economies as to place unequal amounts of economic and political power in the hands of various private decision makers. Both problems require the creation of a national consensus that will approve a continuous monitoring of the nation's economic trends. This monitoring would be accompanied by collective gathering and processing of information relating to these trends, and the establishment of an open forum for consultation among all the nation's economic and political interest groups with regard to policies and programs designed to deal with the uncertainties of the real world (Gruchy, 1984, p.166). Consequently, for indicative planning to be effective, as it is

consensus based economic planning, it requires that the economic system must not allow the existence of strong independent centers of power. Centers of power should not exist because they would be able to pursue their interests and priorities at the expense of the social benefit expressed in the plan. Capitalist societies dominated by private property and domestic and international capital give rise to independent centers of power which explains why indicative planning was unsuccessful in capitalist societies. In light of the experience of advanced capitalist societies, it is not unreasonable to conclude that this form of economic planning requires an approach to economic policy more in line with that favored by democratic socialists in market socialism.

Although the market socialist model aimed to reproduce the accountability of capitalism, it also envisaged new forms of accountability. In particular, it incorporated national allocative planning and workers' election of management, which had been inhibited under capitalism due to the power of domestic and international capital. One of the problems with a high concentration of private ownership in capitalist societies was its consequent influence on the political process. Under the market socialist model, this was less likely to happen. Also the media would be less likely to be influenced by particular interests. Therefore, market socialists argue that with the elimination of some and the effective control of the remaining centers of power, market socialism can achieve equality of opportunity for self-realization, welfare, political influence and social status within a market-planned economy.

### **Internet sites**

Hayek Center for Multidisciplinary Research

[hayekcenter.gregransom.com/](http://hayekcenter.gregransom.com/)

Ludwig von Mises Institute [www.mises.org](http://www.mises.org)

Union of Radical Political Economists

[www.urpe.org/index.html](http://www.urpe.org/index.html)

World Socialist Web Site: [www.wsws.org/](http://www.wsws.org/)

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## Feminist Policies

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### **Introduction and definitions**

How can we define feminism? From the outside we should stress that feminism is a plural movement, with a variety of schools. In general, feminism is both an intellectual perspective as well as a political movement that provides a critique of society, with a special focus on the relative positions of women and men. But this critique takes many different forms. One classical definition considers feminism as a movement to end sexist oppression (e.g. Hooks 1984,2000). This definition focuses on structural aspects of culture and society, thereby acknowledging that both men and women can and do perpetuate these sexist structures. Some feminists stress the central role of people's behavior in this oppression; others highlight societal structures such as the nature of global capitalism. Some feminists locate the core source of this oppression in sexuality, others in the economic system or in cultural beliefs and ideologies.

Many feminists prefer not to use the word 'oppression', as it evokes an image of powerless women who are only victims rather than also agents of change. An alternative definition of feminism centers around the notion of gender justice. This definition has the advantage that it allows for a wide variety of causes of injustices. In addition, if justice is understood to be the main overarching concern of feminism, then it becomes obvious that feminism is an integrated part of a wider movement fighting injustice in all its dimensions, including injustices based on 'race', class, ethnicity, religion, disability, sexual orientation, and so forth. However, many affluent white upper-class heterosexual feminists are often less interested in injustice

related to class, 'race' or sexual orientation or issues regarding justice on a global scale. Their views of feminism are likely to be much narrower than the definition above, and they are often criticized by women who do not fit into this category. Black feminists have criticized mainstream feminism for ignoring how sexism and racism interact, and for developing 'white' feminist theories. They have also argued that it is often illusionary to think that all women can be assumed to show solidarity with other women, because black and white women have different stakes in race relations, and racial tensions sometimes trump gender concerns. Similarly, lesbian feminists have criticized heterosexual feminists for privileging the heterosexual family, to the detriment of the well-being of lesbians and their families.

While feminists focus primarily and mainly on the way women are disadvantaged in society, some also argue that the same structures or cultural features that create injustices towards women, sometimes also create different injustices towards men. For example, ideologies of good motherhood put the primary responsibility for raising children with mothers rather than fathers, but in some countries the same ideology will negatively affect the chances of fathers to gain equal custody over their children, even if they were equally involved in childrearing. In other countries, however, fathers are always given custody, even if the mothers were full time responsible for childcare. Cultures impose gendered norms on both men and women, and in some societies cultural norms defining appropriate forms of masculinity are more restrictive than those of femininity. Nevertheless, given that in all societies women as a group face on balance significantly more disadvantages and injustices than men (e.g., Tinker 1990; UNDP 1993; Rhode 1997; Robeyns 2003), most strands of feminisms primarily focus on the

injustices against women. Recently it has also been recognized that injustices also derive from the specific prohibition of, and discrimination against transsexuality (e.g. McCloskey 1999). The position and problems of transsexuals makes clear that only two different sexes are recognized – one has to be either strictly a man or a woman, whereas for some people this rigidity violates their physiological and psychological identity.

Note that the representation of feminism in the mass media and in many people's minds is often very different from what feminists actually stand for. One widespread prejudice is that feminism would be anti-men; another error is that feminists are women who aspire to be like men. In academic circles, where people are more likely to read what feminists actually write, the biases and prejudices against feminism are less strong, or at least less overt.

Due to the many faces of feminism, and the wide range of areas in which feminist policy interventions have been made or could be made, it will not be possible to do much more than giving some very brief introduction into the core theoretical concepts of feminist studies, highlight some aspects of the current nature of gender injustice, and present two case studies (prostitution, and work-family balance). For further reading, including historical background and a detailed description of the different typologies and streams of feminism, see the *Routledge International Encyclopedia of Women: Global Women's Issues and Knowledge* (Kramarae and Spender 2000).

### **Core Concepts and Methodologies**

In its analysis of the position of women and men in society, feminist theory relies on a number of core theoretical concepts.

The first set of concepts are sex and gender, whereby sex refers to those aspects of men and women that are biologically given,

whereas gender is the cultural meaning attached to those sex differences. Some sex-differences are uncontested, e.g. that only women can bear children. Other sex differences are debated: for example, while all scholars would agree that men and women differ with respect to hormones, some would stress that these levels are influenced by the social environment, and others would stress that the differences within each sex are very large.

Some literature exposes how the production and classification of the natural (e.g. the body) and the cultural is a political process related to the hierarchical distinctions between men and women. Indeed it has been shown how often the “natural” is the name given to the sphere of traditionally female activities and “cultural” to what is traditionally men's competence. The “natural” is generally conceptualized as something that can be taken for granted, and that is not produced with labor, and at the same time it is to be mastered and dominated by what is considered as the “cultural”.

In addition, there is profound disagreement regarding the societal and policy implications of what are considered sex-differences, with some arguing that the biological differences are misused as excuses to retain the sexist structures in society (Kimmel 2000), and others arguing that these biological or innate differences between the sexes are much more important in explaining differences in men's and women's positions in society than social policies (Goldberg 1993). These two positions lead to different policy implications: one could argue that the differences between men and women are small, and that policies should try to treat men and women as similar as possible, or one could argue that the differences between men and women should be celebrated and recognized by policies. Among those who take the latter view, some think that the differences between men and

women are biological or in another way essentialist and unalterable, while others situate the difference more in psychological or psycho-analytical terms. Feminists are situated all along the spectrum from sameness to essentialist differences, which is one major reason why there is not just one feminism, but many different types of feminisms.

Feminist analyses and policy making is characterized by a strong interdisciplinary and “holistic” methodology. One of the first projects that feminist scholars carried out was to develop critiques of the mainstream and canons in academic disciplines, and to put into question the methodological disciplining that takes place when students and researchers are being educated and trained. Some feminist scholars have argued against the idea that the most important concern in research should be to safeguard objectivity, which would require that scholars are completely detached from their objects of study, and should exclusively use their reason, rather than also their emotions and intuitions. This has, among other things, lead to an increasing domination of quantitative methods in the social sciences (esp. economics), whereby qualitative methods are regarded as unscientific. Feminist scholars have argued that not everything can be quantified, and that many quantitative studies that give the impression of being objective, are instead biased by the questions they ask, the underlying androcentric assumptions, the dimensions they leave out, and so forth. In general, there is much more debate on the philosophy and politics of knowledge production among feminist scholars than among mainstream scholars.

Feminists have also critiqued the lack of interdisciplinary work in the academic world. Especially in economics, a rigid –and for many even dogmatic– view on how one should do research has lead to an increased narrowness of the research being produced

(Nelson 1996). For gender issues, this is highly problematic, as gender is a social phenomena that has both socio-economic as well as socio-symbolic dimensions. If one focuses narrowly on the economic side of a gendered phenomenon (such as gender inequality on the labor market), one will not be able to understand what the real causes of this inequality are. Feminist scholars and policy makers therefore generally use interdisciplinary analyses, and “holistic” methods that try to gain insights from different perspectives, e.g. by combining quantitative with qualitative analyses.

### **Feminist Issues in Overtly Sexist Communities**

In virtually all communities, women do not have de facto equal rights to men, let alone an equal quality of life or equal freedom. However, women in overtly sexist communities are much worse off than women in less overtly sexist communities. Some feminists will be cautious to make such statements, either due to the fear of being instrumentally used for imperialistic purposes, or because they hold strongly relativist epistemological views (in other words, they believe that different situations, especially between different cultures, can never be compared).

For a start, more than 100 million women are ‘missing’ from the population statistics – a fact that has never received a lot of political or media attention (Sen 1992, 2003; Klasen en Wink 2003). These ‘missing women’ are partly caused by female infanticide, and increasingly also by sex-specific abortions. While some had hoped that increased material development would automatically eradicate female infanticide, its effect is rather a broader access to prenatal fetus scans which facilitate sex-specific abortions. As long as a woman is culturally or economically considered not to be worth the same as a man,

such practices will not cease to take place. Political and social action aiming at cultural change and at combating more materially grounded reasons for women's lesser social value are needed to end this practice.

In most countries, women are not granted the same legal rights as men, as is made plainly clear in the research of human rights organizations such as Amnesty International. Vulnerable women, such as those living in poverty, refugees or migrant women, are more likely than other women, let alone men, to be sexually abused, sold, raped or otherwise deprived of some basic human rights. In some countries, women have the legal status of minors; or female genital mutilation puts their lives and sexual pleasure at risk. Some regions of the world know practices of female seclusion, where women are not allowed to leave the house unaccompanied by a male family member. There are also many economic inequalities and injustices, such as the fact that women are excluded from certain labor markets, or are excluded from the most lucrative parts of a production process.

Given that in some poor countries the majority of women live in rural areas and live from agricultural production, the gender bias in land entitlement is a major feminist issue. The obstacles to women's access to land lie in a variety of factors. Bina Agarwal (2002) argues that inheritance laws often strongly favor male heirs. In addition, gendered social norms also play a role, as the notion of a "good sister" might require that the female heir forgoes her share of the land to her brothers. In addition, many government functionaries, living in the same sexist culture, are only adding to the gender inequality in land ownership, for example by discouraging female heirs to claim their legal share. Higher level governments often transfer land mostly to men, as they (often wrongly) assume that men are the

breadwinners while women are only helping out in the household. Agarwal's research (2002,2003) clearly shows that the unequal land entitlements of women can only be explained by looking at a wide range of factors that span from religion to culture to law to government policy. Therefore her policy recommendations, which are for the Indian context, cover all of these terrains. However, a volume on gender and land rights edited by Shahra Razavi (2003) clearly shows that there can be no general policy prescriptions for countries with a significant rural population, as the local social, legal, cultural and historical context is very important to understand the causes of unequal land entitlements and the effectiveness of the different policy options. Moreover, the global factors that impact on gender inequalities in land rights and entitlements can also be different.

Recent overviews of the situation of women in the world clearly show that there is a long list of problems (for more detail see UNDP 1993, Kramarae and Spender 2000, Molyneux and Razavi 2003).

### **Feminist Issues in Covertly Sexist Communities**

In covertly sexist communities, women's equal worth with men is generally written in the laws, and is part of the general discourse. Therefore one would think that these communities are feminism-friendly. Moreover, many people believe that feminism was an important struggle of the past, but that there is no longer any need for it (Rhode 1997:1-20; Saul 2003:1). This reasoning is partly based on the idea that women have now formally the same rights as men, and that in Western cultures women and men are considered to be equal. Plain cases of discrimination from the past, for example that a female teacher in a Belgian Catholic school who married automatically had to resign, or

that women were paid less than men for exactly the same work, are no longer considered morally or legally acceptable. By law, women have the same rights as men. In short, most people in those societies believe that men and women are treated equally, and sexism belongs to the past. In this view, any gender inequalities that are still observed are not problematic, because they are due to the fact that women make different choices – yet they do have the same opportunities as men.

Feminist scholarship shows that this popular view about gender equality is overtly optimistic and is contradicted by recent evidence. For one thing, gender discrimination is very much alive, but in most cases not in its overtly and intentional form that it once had. Discrimination continues to work through the gendered stereotypes that both men and women hold, and by which they regard women as less competent in activities that are culturally regarded as masculine (such as many forms of paid work), while men are seen as less competent in so-called feminine activities, such as caring. There is plenty of evidence that these stereotypes are still operating and are hard to eliminate from our cognitive processes, and that they do result in unintentional but significant gender discrimination (Valian 1999). For example, during the allocation of public research funding in the biomedical sciences in Sweden in 1995, women had to be two and a half times more qualified than men (on generally accepted objective indicators of past performance) to be awarded a research grant (Wennerås and Wold 1998). Still, Sweden is generally regarded as one of the most feminist states in the world. In sum, even on a minimal understanding of gender equality as the absence of discrimination of women, the available evidence suggests that no society has reached such a situation of gender equality.

Moreover, many feminist activists and scholars have argued that equal formal rights are by far not sufficient to create a gender just society. Even when the laws are just, the legal practice may be biased, the law may be difficult to enforce, people may rely on stereotypes and be prejudiced, or institutions may be gender biased, as will be illustrated below.

### **Areas of Feminist Policies**

Feminist concerns stretch out over almost every conceivable domain of life. There are issues that concern girls or women directly, such as policies to reduce women's mortality rate at childbirth, the criminalization or legalization of abortion, or gender inequalities in legal rights. We already mentioned the issue of female infanticide, and sex-specific abortions. Feminist policies are also needed to combat violence against women – including domestic violence. Rape remains an issue of feminist concern, especially since it has not ceased to be used as a weapon of war. Policies are needed in the area of education, as in many countries boys are much more likely to be able to go to school than their sisters. In some countries gendered traditions make it more likely that girls have to work at home while their brothers go to school; in other countries sexual violence and the HIV/AIDS pandemic, and the lack of any effective policies to eliminate this violence, make it dangerous for girls to go to school (Unterhalter 2003).

In post-industrial societies, the labor market and other social institutions have typically been designed to fit the average male, who has no significant caring responsibilities and is not the person who is the main adult responsible for the household. Thus, an important task of feminist policies is to redesign those institutions to make them less androcentric, and inclusive for women as well. For example, in countries where the

labor market is structured around full-time versus small part-time jobs, women with child care responsibilities will face severe obstacles to combine their parental duties with financial independence and/or holding a job which allows for a career or personal development. This will even be more the case if other social institutions, such as schools, take for granted that one parent doesn't have a full-time job (for example, if the school hours are short, or if it is expected that a parent gives the children a warm meal at lunchtime, as is the case in most Dutch and German schools). Some European welfare states are experimenting with a number of policies that should allow for gender equality, such as parental leave, or legal rights to reduced working hours for parents with small children. However, feminist scholars are divided on which measures are most effective, and also disagree about the implicit values and ideals in such policies (e.g. Daly and Rake 2003, Helburn and Bergmann 2002, Williams 2000). The second case study that we will discuss below will expand on these tensions.

In all societies, sexuality remains gendered, with men's "sexual needs" being regarded as the norm, whereas women are constrained in their well-being and indeed often being held solely responsible for joint behavior or indeed sexual attacks on them, as the literature on rape points out. In some countries these double and gendered standards are embedded in the law, whereas in other countries the law may be gender neutral, but the legal practice is not (e.g. Kennedy 1993).

Even though this list is only very partial and incomplete, it makes clear that gender issues are relevant in many areas of life, and that therefore many public policies can benefit from feminist insights. As it is impossible to discuss all the above areas in detail, we will focus in what follows on two case studies. The first case study is prostitution. This is an

important case study for feminist policies, as it shows that different feminist views are often in conflict, and that some basic ideas, such as the firm distinction between the sexual sphere and the economy, can not hold. The second case study is work-family balance. This case study will illustrate that feminists can have conflicting views on which policies are best. Moreover, countries have pursued very different policies, which has lead to considerable cross-national differences of indicators regarding children's well-being, gender inequality, and freedom for parents to choose whether and how to combine paid employment with caring responsibilities.

### **Feminist Policies on Prostitution**

Gender is clearly a central aspect of prostitution. Worldwide, almost all clients are men, and the large majority of those working in prostitution are women and Male to Female (MtF) transsexuals. Yet, policy approaches and theories often disregard the aspects of conflict and negotiation among genders and within genders, which are always present in this otherwise very diverse activity. Feminists have worked to create a political and theoretical space for these dimensions of conflict and negotiation (Outshoorn 2004). This is a space that necessarily calls for the inclusion of other axes of social dissymmetry such as class and "race" as they shape gender without undermining its consistency. Specifically, the feminist contribution allows us to look at prostitution as a modifiable reality placing it within a larger frame of asymmetric sexual-economic exchanges between women and men.

Prostitution constitutes a direct challenge to the ways in which sexuality and work are organized and understood in most contemporary societies. As economics and sexuality are two of the main objects of feminist critique, prostitution inevitably is a

highly controversial issue among feminists themselves.

### **Not only Gender**

In the context of contemporary global migrations, issues relating to prostitution take particular meanings in relation to gendered movements and borders. Namely the total or partial non-recognition of prostitution as a legitimate activity emerges as being central to denying residence permits to foreign women and transsexuals. Even in the Netherlands, where prostitution is legally recognized as equal to other professions, as a general rule there is no possibility for non-European Union (EU) migrants to legally work in the industry. Also some calls for legalisation of prostitution, for instance in Eastern Europe and in South-Eastern Asia, including registration and mandatory medical health control, have been denounced as being inspired by the wish of more control of the mostly female workers.

These policies are sometimes justified on the grounds of feminist arguments for the protection of women who are considered at risk of being “trafficked” due to their poverty or because they are seen as less emancipated (Barry 1995). Nevertheless, these have been exposed by some feminists as being neo-colonialist and anti-migration arguments (Augustín 2003; Doezeema 2000). It is argued that they assume an essentialistic difference between women from the South and women from the North by attributing only victimization to the former and only agency to the latter. In fact they prevent women, transsexuals and in particular sex workers from legally migrating (Thorbeck and Pattanaik 2002). According to this alternative view, anti-trafficking arguments claim to protect the women from the South, but in fact they should be seen as instruments for Northern women to protect their privileged position vis-à-vis foreign women.

### **Who are the “Women”?**

The earliest public discussions on prostitution by feminists started in England in the 1860s against the Contagious Diseases Acts. Based on public health arguments, these laws provided for the compulsory vaginal inspection of women “suspected” of prostitution, most likely to be unmarried working-class women. In the campaign against the Acts, one group of feminists allied with the social purity movement and started to ask for the abolition of prostitution per se. Another group, also calling themselves feminists, remained instead closer to the original position promoted by Josephine Butler and supported the working women calling for the abolition of state regulations on prostitution (Walkowitz 1980). In short, since that time it has been clear that “women's” interest in relation to prostitution cannot be taken as self-evident. It has been documented for instance how a number of feminist policies are to the particular advantage of the “good girls”, who are distancing themselves from “whores”. This attitude of “good girls” is certainly understandable, because the “whore stigma” does not apply exclusively to sex workers, but is rather as a general threat for all transgressive women (Pheterson 1996). Care should therefore be taken not to circularly define “women” as “non-prostitutes” in policy debates. These worries are important given that prostitutes and sex workers are usually excluded from feminist and non-feminist public debates where non-prostitute women often speak on their behalf as if they were unable to speak for themselves.

### **Prostitution as Modifiable**

The original contribution of feminists has been to criticize the traditional attitude that sees prostitution as essentially unmodifiable in its economic form and in its social and

psychic meaning. Prostitution is traditionally seen as inevitably implying the exploitation of the mostly female workers, their stigmatization and their relegation to a position of non-citizens and non-subjects. In such a perspective, prostitution appears as publicly unacceptable to contemporary democracies. Slight variations of this position aim at keeping the problematic aspects of prostitution *within* its sphere. Problems are mostly understood as being moral, sexual, and health issues. In terms of contemporary policies, invariably these analyses seek either to eliminate prostitution, or to isolate and to hide it.

Following the developments of prostitutes' and sex workers' movements since the end of the 1970s (Pheterson 1989), this "prostitution as unmodifiable" paradigm sometimes recognizes the distinction between "voluntary" and "forced" prostitution (often also called "trafficking"). Nevertheless, since it is usually based on the *a priori* individual choice/non choice of practicing prostitution, this distinction runs the risk of translating into the legal, or at least moral, condemnation of those who consciously make the decision to work in prostitution. The abuses they undergo are fundamentally considered to be the natural consequences of the work they have chosen, meaning it is their own fault.

Feminism has criticized naturalized social relations, arguing that they are historically changeable. Appropriately translated into contemporary prostitution policies, this has opened the way to policies which seek to change the sex industry without trying to eliminate or hide it. Concrete support from this feminist position goes to the decriminalisation of prostitution, the "harm reduction" interventions, and to some forms of neo-regulamentarism which are seen as promoting women's emancipation and labor rights (Kempadoo and Doezema 1998, Truong 1990). In this alternative approach

prostitution has been looked at as an institution similarly for instance to marriage and waged labor (O'Connell Davidson 1998). The focus is not on whether the sex industry will grow, but rather on the quality of social life in the prostitution market and on the possibilities of resistance and emancipation existing within a practice so strongly situated in the stratified sexual and socio-economic systems (Rubin 1984).

The difference between "voluntary" and "forced" prostitution is in this critical line addressed in terms of degree, as discernible in the conditions in which the work is effectively performed (Wijers and Lap-Chew 1997). "Slavery" has been treated with the same analytical tools as those applied to the rest of labor, and ways have been found to explore and fight its emergence by placing labor relationships in a larger framework along with mobility and population control.

### **A Divisive Issue for Feminists**

Alternative views have been developed by feminists who tend towards the "prostitution as unmodifiable" account. They see prostitution as inherently bad for women, not only in itself but also as a symbol for the rest of gendered relations in the society at large (Pateman 1988). They conceive the selling of the sexual body as the ultimate form of submission for women (Jeffrey 1997). Their interpretation is that women are pushed into prostitution by a system that objectifies them and does not offer other viable economic alternatives. Once in prostitution they can only find worst exclusion and pain (Barry 1995). Prostitutes sell off their subjectivity, and in particular their "gender", their being a woman (Pateman 1988). Clients on the other hand are viewed as abusive *per se*, fundamentally equivalent to rapers.

In practice, these feminist thinkers and activists consider that non-prostitution is preferable to prostitution in all cases. They try



to discourage prostitution and to reduce its practicability. Although this position is often supporting decriminalisation, some local actions have included disturbing clients, for instance fining them, and increased public control on prostitutes.

Along this line, the 1999 Swedish law is sometimes presented as a feminist law. It is considered feminist because it has been actively promoted by female politicians and because it criminalizes the buying of sexual services on the basis that prostitution reproduces in all cases the unequal power balance between men and women. And yet, a number of feminists have shown how that law in fact works as a prohibitionist policy. As such, they stress, it puts women involved in prostitution in an even more invisible, marginal, and dangerous position (Thorbeck and Pattanaik 2002). Violence in prostitution has increased since women need to be quicker and less selective with their clients. In such a context sex workers' power has diminished both in the negotiation with clients and in the public debate, since sex workers *officially* do not exist. Besides, specific prevention and health programs have been cut.

Distrust of this law also comes from those considering these effects as legitimate costs to be paid for a reduction of prostitution, since the market has proved able to reorganize itself, especially through the internet and through sex tourism to neighboring countries.

Larger objections to this kind of feminist models derive from the variety of experiences of women, men, and transgender people in prostitution (Kempadoo and Doezema 1998). Although prostitution emerges as being in general a stressful activity, and not a "normal job", violence is seen as being only related to particular conditions, and alienation is not reported as being stronger than in other less remunerative occupations.

In addition, feminist social scientists and economists have argued that selling and

buying "gender" (i.e. gendered services) is not unique to prostitution (Pateman 1988, Tabet 1991, Wijers and Lap-Chew 1997). For instance, caring and relational services within the family or in the market all mobilize service providers' gendered skills and service users' gendered interests. Notwithstanding, it seems too radical to most feminists to condemn these exchanges per se, and the market is in these cases largely accepted as a possible emancipating way for women. Furthermore, the strategic use of the sexual body in exchange for money or material compensation is reported as being a relatively empowering experience for some, not only in the context of prostitution, but also in other relationships such as marriage and dating.

Significantly, people working in prostitution are able to make the difference between a rape - whether by a client or not - and a paid sexual act. The punishability of sexual violence within prostitution is indeed one of the key struggles of sex workers' rights activists (Pheterson 1989). The debate over this crime is equivalent to the debate over the recognition that prostitution can be about negotiation and not exclusively about violence.

### **How Sexuality Meets Economy**

The diversity among feminist policies is not fully understandable through the well-known legal framework that classifies abolitionist, prohibitionist, regulationist, and decriminalization approaches to prostitution. The different feminist positions on prostitution are instead usually divided into "abolitionist" and "sex work". The first refers to those who see prostitutes as victims (of men, of poverty, of sexual violence, etc.) and take as an end to help all of them to quit prostitution. The latter indicates those who see prostitution as one of the forms of sexualized labor, and thus seek to transform it to the advantage of the sex workers by

improving the conditions in which it is practiced and thought of,

Yet, the “abolitionist” versus “sex work” categorization is also unsatisfying, since it is often used in a naive way as equivalent for “anti” and “pro” prostitution. This polemical polarization reflects the fact that prostitution has become such an important issue for feminists as to represent a cause of strong divisions within the political and the theoretical feminist movement. Even the classical differences among feminist policies, such as socialist, liberal, and radical, are not relevant here. Policies on prostitution have become a specific line of division within feminism.

The reason why that is, may be found in that prostitution is a threat to the understanding of two key objects of feminist policies: sexuality and work. The way in which “the sexual” and “the economic” *can* interact in a transparent contractual form between prostitute and client has been identified as constituting the original and indeed definitional feature of prostitution. At the same time this is also understood as causing its illegitimacy in a sexist society: women cannot explicitly ask for money for sexual services they are supposed to provide otherwise (Tabet 1991, Pheterson 1996). Because of this potential form of negotiation, prostitution represents an open challenge to the distinction between on the one hand the sphere of sex, the private and the unproductive, versus the sphere of work, the public, and the productive. This separation has been exposed by some feminists as central to a strategy of denying the caring/affective/reproductive labor of women the financial and status rewards of work (Tabet 1991, Zatz 1997). At the same time, a large part of feminist policies have been traditionally built upon this same idea - or ideal - of sexuality and work as two separate spheres. In this context it is difficult to

include the reality of prostitution without a complete questioning of one's feminist framework.

### **The Problem of Work-Family Balance**

In contemporary post-agrarian societies, one of the most pressing problems for many women is how to combine employment with caring for children, and increasingly also for dependent elderly. The economic transformations of these societies over the last two centuries have been such that most women can no longer combine their work while simultaneously looking after their children, which most of them did when most families were still farmers and thus worked where they were living and produced for their own living. Moreover, a number of other factors have led to socio-cultural changes that give women much more real access to the labor market, and autonomy on whether and when to have children: the emancipating effects of the employment of women during the Second World War, the shift from an industrial economy to a services-based economy which increased the demand for women's labor, the introduction of the birth-control pill in the 1960s, and cultural changes which have given women more freedom in deciding which kind of life to live (Blau, Ferber and Winkler 2002).

But these socio-economic transformations have created a problem for parents to hold jobs which keep them out of poverty and do not excessively jeopardize their professional ambitions, while at the same time having enough time to care for their children. Of all socio-demographic groups, parents with young children experience the most time-pressure. However, this time pressure is in most countries worse for mothers than for fathers, as employed mothers are the group who work the most total hours (i.e. paid and unpaid), and have least time for themselves (Gershuny 2000). Large proportions (roughly

between 75 and 90%) of parents in post-industrial societies report that they would like more time with their families (Gornick and Meyers 2003, 81).

Time is not the only problem for parents. In some affluent societies with very poor welfare state provisions, especially the USA and the UK, having children is a significant factor that lowers the family's STANDARD OF LIVING. Many working parents are faced with the difficult choice between being able to care and being able to earn money. Low-paid parents who work are often not able to spend sufficient time with their children, or have to bring them to low-quality child care, or parents take alternating shifts on the labor markets which also takes its toll on family life and the health of its members (Gornick and Meyers 2003). If parents instead choose to provide the care themselves, they lose out on labor income, and are at severe risk to move (deeper) into poverty.

Some policy makers and researchers have tried to analyze this problem in gender-neutral terms. But this is deceiving, as there is a strong gender dimension to the problem of work-family balance. In all countries, women do the lion's share of unpaid work. Upon the birth of a child, it is almost always the mother who adapts her employment situation (hours and/or type of job) to accommodate the increased need for unpaid work at home. (Gornick and Meyers). This makes women vulnerable within the marriage. It also makes women very vulnerable in case the marriage breaks down, as their earnings-generating capacities have been weakened or eroded in the time they had weaker labor market attachments. In spite of divorce regulations that require the parent who had the greater income (almost always the father) to pay alimony to the other parent and the children, there is strong empirical evidence that women's and children's STANDARD OF LIVING significantly drops upon divorce (e.g. Jarvis

and Jenkins 1999). Moreover, most women also have professional aspirations, and prefer to share the unpaid work and care work more equally with their male partners. But this has proven to be an uphill battle. Even though many women would like to have a more equal division of paid and unpaid work within the household, men tend to resist this claim, and women often give up their claims when men continue to resist (Hochschild 1990; Komter 1989). Many dominant notions of gender still associate household work and care with femininity, and thus one reason why men refuse to do a more equitable share of household work and caring is that it might endanger their sense of masculinity. According to Julie Brines (1994), this threat to men's masculinity would explain why unemployed American men do the least household work of all men, as their unemployment already hurt their masculine self-identity, which they would not want to be further jeopardized by doing 'feminine' work in the household.

There are thus two interlinked problems created by the pressure that both employment and care responsibilities put on families. One is that parents (and other adults caring for vulnerable people) have a greater need for both household income and for time to care, compared with people without caring responsibilities. The second problem is that this pressure on families either creates or reinforces a gendered division of labor in the household, and correspondingly typical 'female' patterns of employment on the labor market (part-time work, non-standard hours, etc). which create socio-economic disadvantages and vulnerabilities for mothers.

### **Policies for Balancing Care and Work**

The challenge for feminist policy makers therefore is to design the appropriate policies and regulations that can address both these problems simultaneously. There have been three types of policy proposals. The first type

focuses on employment, and argues that women should strive to gain equality with men on the labor market. The second type focuses on caring work, and stresses that society should support women to care for their children. The third type proposes that policies should allow both men and women to care and to work, and strives for an “dual-earner-dual-carer” society (Fraser 1994; Gornick & Meyers 2003). All three models have to a more or lesser extent been implemented in different societies: the “employment model” underlies social policies and labor market structures in the USA, the “care work” policies has elements some continental welfare states like Germany, and the “dual-earner-dual-carer” model best describes the social arrangements in the Scandinavian countries (Gornick and Meyers 2003).

Policies that focus on gender equality on the labor market aim at removing any barriers for women to take part in the employment process on equal terms with men. Thus, these policies would combat employment discrimination and arrange for the provision of child care facilities – either provided through the market or through the public or a (semi-)regulated sector. In countries with a significant low-wage sector, especially the USA, much child care is performed via the private market. However, while the evidence is not entirely conclusive, there is doubt about the quality of the child care in this unregulated private sector. In countries with minimum wage regulations, and relatively generous unemployment and income support systems, such an unregulated child care market is much smaller or virtually absent. Many of these countries, such as the Belgium, Denmark, Finland, France, Norway and Sweden, have a state-regulated and state-subsidized child care sector. This both guarantees the quality of the child care, and makes it affordable for parents to buy child

care services and hence to hold on to their jobs.

The opposite model argues that women do want to care for their children themselves, and that the government should give women the financial means to do so. One prominent version of this model stresses that women are different from men, and that most women themselves prefer to care for their children, rather than to hold a job when their children are young. In its most pure form, this model would lead to a so-called “mother’s wage”. Other feminist groups advocate “wages for housework”, not necessarily because women would *want* to do household and care work but rather because it is important that this work gets done and therefore society should make it financially possible to do so. While some “care-feminists” or “difference-feminists” advocate this care-focused model, many feminists are weary that the strong financial incentives for women to stay at home would make it hard for them to arrange an alternative division of labor within the household in case they prefer to hold a job, that it would make them economically vulnerable within and outside the household, and that it could create (or strengthen) cultural norms about what a good mother is supposed to do. Moreover, this model has been advocated by extreme-right and conservative religious groups, and most feminist are very worried about the very restrictive views that these groups have about women’s proper role in society.

Nevertheless, despite these concerns with the care-focused model, many feminists do recognize the time pressures that parents suffer, and recognize the beneficial effects on both children’s well-being and on family relations if the parents can spend enough time with their children and care for them. The challenge for feminist policies is thus how to create genuine equal opportunities for both men and women at home and on the labor

market, while at the same time creating social structures and welfare state services transfers to support parents. The end goal would be a society in which both men and women would take an equal responsibility for caring and for working on the labor market, and where the government supports parents by providing them with paid maternity and parental leave, good quality child care facilities, free access to state-funded pre-schools, and so forth. It would also require that parents should be allowed to work large part-time job, e.g. 25 to 35 hours, rather than the long (40+) hours that parents now work in countries with poor policies to combine work and care, such as the USA and the UK. The “dual-earner-dual-carer” proposal also requires cultural changes. Even in those societies that now come closest to this model (the Nordic European countries) there is still a significant gendered division of labor, and a large gender segregation on the labor market which sorts most women into large part-time (often public service) jobs which are friendly to parents, and most men into parts of the economy that much more resemble the competitive full-time jobs. Within the households, men and women still create a gendered division of labor. Thus, to reach the “dual-earner-dual-carer” society, most men will have to become willing to take equal responsibility for care and the household work. And some women will also need to change their attitudes and allow men to care.

Moreover, this model has generated its own criticism. Alstott (2004) has argued that parents should not expect from employers to pick up the bill of parenthood, by allowing flexible working hours and accommodating extended parental leaves. Some economists have also argued along these lines, saying that these policies would be harmful to the economies, especially now that economies need to become more competitive in order to be able to compete with the increasing

competition worldwide. Gornick and Meyers (2003) have argued that the USA has currently the least provisions for parents from all the post-industrialized affluent societies, because in American culture the family is largely seen as a private business, for which society should not bear responsibility. This is related to a more fundamental and theoretical point: why should society at large provide any support for parents at all? Why should people who are not able or not willing to have children pick up the bill of people who have chosen to have children, and also benefit from the joys that this brings? While several arguments have been developed for why parents should be supported by society (e.g. Alstott 2004, Folbre 1994), this is still a contested issue. Most academic feminists, including many feminists without children, take the position that society should support parents and children. But at the grassroots level support for caring responsibilities is also an issue that sometimes divides feminists with and without children, or with and without caring responsibilities.

## **Conclusion**

Feminism has historically developed from a movement concerned with suffrage and equal legal rights, over issues of sexual and economic freedom, to a wide view that criticizes virtually all aspects of society which limit men, women and transgender people in their personal flourishing. While feminists – as well as other groups of people – are divided on the issue of to what extent men and women are intrinsically different and what this implies for claims about injustice, they are united in their views that right now no society treats its women as well as its men. These injustices can be very different from one society to the other, although some issues, such as domestic violence, or discrimination against women on the labor markets are present in all societies.

For most gender injustices, there are always policies which could weaken the injustice either directly, or indirectly. However, in reality governmental policies sometimes don't make life easier for women, and (in some societies more than in others) politicians and civil servants often aggravate the situation by acting upon their own gendered prejudices and stereotypes.

As a consequence, many feminists either have only limited hope that policies will ultimately make our world gender just, or either think that such policies should at best be seen as complementary to a cultural change which is necessary to change the gendered nature of society. Such feminist grassroots movements and other collectives, which are active in areas from prostitution, over campaigns on land right reform, to the redesign of the European welfare state, engage in forms of social criticism that are a necessary part of any type of feminist policy or governance (Ackerly 2000). The path towards a gender just world is long and thorny, and both feminist policies as well as feminist social action and criticism will be necessary to reach a society in which women are no longer disadvantaged.

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## Governance

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### Introduction

“Governance” has emerged in the social sciences and public policies only in the last two decades, although, according to Webster’s Collegiate Dictionary, the word is rooted in Middle English. There, however, it was identified with *government*, i.e. with state authorities. Nevertheless, it was hardly used until recently.

With its re-invention, governance is no longer confined to public government but it now reflects renewed interest in diversity and *comparative* structures, processes and performance of *allocation mechanisms*, (economic) systems, or organisational forms through which economic agents interact and get *coordinated*. The shift is indicative of the fact that the ideal, competitive “*market*”, largely viewed as the optimal system and measuring-rod by mainstream economics and economic policies, is far from being *the* problem-solving device in a complex world and, therefore, has to be complemented, (re-)embedded or substituted by competing forms of coordination. *Hierarchy* (bureaucracy, private and public), *network* forms of *cooperation* and their *hybrid* forms are at stake. “Governance” now pertains to diverse forms of coordination of agents beyond the ideal “*market*”.

The issue of “allocation” and distribution of resources, information, power, rights and duties, as well as income and wealth, has become more open with the recognition that forms of coordination can be quite diverse. Moreover, each coordination mechanism may have a number of sub-versions. The problem of economic coordination and performance, thus, can no longer be fruitfully dealt with in the axiomatic world of the “pure” logic of (general) “*market*” equilibrium models.

The new relevance of governance expresses the fact that we face complex economic conditions that call for more adequate forms of coordination *beyond* (1) the “*market*”, (2) the “black box” of the (isolated) *firm* and (3) a largely non-reflexive *state*. In a genuinely complex world, only forms of coordination which can deal with this increased complexity are capable of maintaining and improving economic performance. Starting from a simple “baseline” for any coordination mechanism, i.e. structure + governance = performance, the economic problem, basically, is to work through a potentially great number of combinations of structural forms of these mechanisms, procedural rules, and resulting levels of economic efficacy.

Here, the *rules that shape the processes which may lead to coordination*, given a certain structure, and in order to generate high economic performance, are at the core of governance. In other words, governance is about “governing”, “policing” and “managing” problem-solving processes through certain rules and principles. “The challenge is less that of building capacity to compete, but capacity to evolve in order to compete” (Amin & Hausner 1997:28).

“Governance” has experienced proliferating, and increasingly vague meanings. At present, a general definition is not at hand. Any debate on economic development, from LDCs to local communities, from “governance” of the global system to the corporation, from “transitional” economies to “structural reforms” of the welfare state, is increasingly anchored around “governance”, where its vague content is prone to be used or misused in many ways. Against this background, it seems reasonable to anchor its meaning to some *basic theoretical framework*. So we will try to reduce the “complexity” of its use and to focus on a basic explanation.

## Definitions

The *Commission on Global Governance*, in a 1995 report, defined governance as “the sum of the many ways (...) [agents] manage their common affairs. It is a continuing process (...) It includes formal (...) as well as informal arrangements (...)” (Commission on Global Governance 1995, 3). The understanding here seems to be that governance reflects (1) the existence of many agents involved who have (2) common problems to be solved, which in turn requires (3) continuing processes rather than a single “rational” calculus, and which lead to the (4) *emergence of informal institutional arrangements* together with the *deliberate installation of formal institutions*.

In 1997, the United Nations Development Program (UNDP) took a step further by connecting governance with the (continuing) interaction among diverse agents (public, private, commercial and societal) which will lead to a form of lasting cooperation, i.e., that was termed a *network* (United Nations Development Program 1997).

Schmitter has defined governance as “a method/mechanism for dealing with a broad range of problems/conflicts in which actors regularly arrive at mutually ... binding decisions by ... cooperating in the implementation of these decisions” (Schmitter 2002:53, Prakash, Hart 1999:2).

- Governance seems to make sense only if understood in the framework of a
- genuinely socio-economic and societal conception where more than one agent are involved who are
- directly interdependent with each other, i.e., beyond arm’s length relations defined by “markets”, and
- recurrently interacting, in this way entering
- open-ended processes that may result in

- collectively learned and self-sustaining coordination, through institutionalised cooperation, in order to solve
- problems that are common, but nevertheless involve incentive structures that render individual interests mixed, i.e. both partly converging and conflicting.

We can easily agree, therefore, that a definition of “governance as the art of complexity” (Jessop 1997:101), is in contrast to ideal “markets” and hierarchies. Governance can be defined as the *set of principles and rules that determine the interaction processes (i.e., exchange, collective learning) among individual agents in specific allocation mechanisms (i.e., hierarchy, network, “market”, and hybrids), with specific structures, in order to obtain high and increasing levels of performance (i.e., production, innovation).*

We will not delve deeper into specific variants and applications of governance such as “global”, “local” and “multilevel” governance (see Pierre 2000, Wolf 2002). In the following we will stick to a more basic view.

## Economic “Mainstream” Governance Agenda

The objective of neoclassical approaches, and “neo-liberal” political postulates, is the avoidance of the full implications of *complexity*. This applies to the “general market” theory, i.e., GET, to Hayek, and to Coase’s understanding of man-nature interactions, as well as man-to-man bargaining in his theory of social costs. This avoidance saves isolated individualist rationality and, thus, the ideal “market” form of coordination. It even downplays the conception of transaction costs, which can be infinitely high in situations involving strong uncertainty.

From the “neo-liberal” policy perspective, governance is primarily an instrument to increase “market efficiency”. A major application is public administration efficiency, which rationalizes the reduction of welfare state activity. The mainstream’s political programme, therefore, is about ideal, unrestricted property rights, privatisation of any commons, and about generating, by de-regulation, a maximum of liberties in the exercise of such property rights.

### *Hidden Governance of the (Ideal) “Market Economy”*

Ideal “markets” can not cope with complexity originating in direct interdependencies among individual agents, as they are systems of *isolated* individual agents who have only man-good relationships. These relations are determined, in the *general equilibrium* of a “market economy”, through a price vector that depends on the aggregated supply and demand decisions of all isolated sellers and buyers in the different “markets”. Agents are *indirectly interdependent* in that the equilibrium price vector depends on the all other agents taken together.

However, as no decentralised, direct man-to-man interactions (i.e., exchange bargaining) can be accommodated in the GET, mere existence of a general equilibrium of the “market economy” is feasible only by accepting the fiction that any decentralised exchange cannot be allowed before the equilibrium price vector is determined. This, in turn, implies that the “market economy” is governed by a central, authoritarian entity, i.e., the *auctioneer*. The hidden governance of the general equilibrium and optimality conception, with its specific structure, thus, turns out to pervert its initial governance postulates of individualism, perfect liberties and rights into the most centralised and dictatorial governance comprehensible (for a critical discussion of the neoclassical research

programme, s., e.g., Mirowski 1989, Potts 2000, Wellhoener 2002). The “market economy” cannot be comprehended in any sense as an institution-free construct in a pure physical-mechanical analogy. Its governance implications have drastically reduced its applicability and scientific attractiveness and have lead to different approaches within the framework of “free markets”.

### *Hayekian Evolutionary “Market”*

The Hayekian approach relaxes the informational assumptions for the individual agent and, in this way, permits roles for *uncertainty, search* and *adaptation*, which, in turn, comprise an *evolutionary* approach to the “market” mechanism. However, other basic assumptions remain unchanged so that the consideration of complexity, and of different allocation mechanisms, is avoided. In the Hayekian world, “market” prices still contain and diffuse enough information to enable individual agents to effectively search, behave and adapt as isolated and individualistically rational units. Direct interdependencies are avoided, and the decentralised “market” remains the optimal mechanism, in some “evolutionary” sense, though. Under informational restriction, individuals may search and learn, even from each other, but they behave in their isolated, optimal way.

Jessop is right to qualify this as an *a priori reduction of complexity* to save the “market” ideal: “Such incrementalism is sub-optimal from a governance viewpoint because it is based on short-run, localised, ad hoc responses” (Jessop 1997:101). In contrast, mutual direct interdependencies and related “socially complex orders defy both centralized and spontaneous forms of governance” (Amin, Hausner 1997:27), specifically, they defy isolated individualist forms of spontaneous self-governance that ignore the full implications of complexity.

### *Transaction Cost Economics: the “Market” and Corporate Governance*

The transaction cost analysis of governance takes place in the framework of the theory of the firm, that is, between the twin forms of “market” versus “hierarchy” (Zingales 1997). Economising transaction costs and their influential conditions form the basis of the attempt to delimit these two basic governance regimes against each other (Williamson 1996:93ff). The “organisational theory” branch of transaction cost economics pertains to the relative efficiencies of the two mechanisms.

The corporate governance branch, being closer to real-world problems, proceeds from informational limits of some kind (namely bounded rationality) and from the *incompleteness of contracts*. This gives way to *opportunism* and *moral hazard* in *principal-agent* relations. The latter apply to owner/shareholder-management relations, being extended to capital market issues, and to management-employee relations, including labour market issues.

Governance then is defined as “(serving) to mitigate hazards related directly to bounded rationality and opportunism” (Williamson 1996, 12; s. also Zingales 1997, 500f.). According to Williamson, contracting gives rise to “bilateral dependency” (not the other way round!), out of a “large numbers-supply condition” (in the “market” as well as in the commons). Mutual dependency, in turn, specifically when combined with asymmetric information, gives rise to the problem of moral hazard (Williamson 1996, 13ff.). Governance, then, involves the set of mechanisms that shape the ex-post bargaining over the distribution of the economic effects generated in the course of an incomplete contract (also Zingales 1997).

Utilising the theoretical conceptions and ideas of the transaction as the basic unit of

analysis, *limited rationality* and *asymmetric information*, *incomplete property and contracts*, *institutions*, *mutual dependency* (beyond the price relation), (strong) *uncertainty*, *adaptation* and *evolution*, Williamson’s organisational approach to governance contrasts with mainstream analysis and aligns itself with institutional(ist) and evolutionary approaches (Williamson 1996:3ff,93ff).

Nevertheless, with respect to spontaneous, *self-governing* arrangements, Williamson favours a spontaneous competitive “market” which presumably produces arrangements that minimize opportunism/moral hazard in and between companies/employees. This approach clearly supports a neoclassical “‘nearly’ hands-off” political view (Williamson 1996:145ff).

### **Institutional(ist) Governance Agenda**

In the Original Institutional Economics, governance is viewed as a participatory, inclusive and *discursive* form of management to cope with complex economic problems that have a genuinely socio-economic, i.e. societal, character.

In the Twenties and Thirties, Commons developed an elaborate system of governance for a society that is characterised by ubiquitous conflicts of interest over the *bundles of rights and duties* connected with *transactions*. Physical exchange of a “good” consists of a variety of transactions involving different rights and duties, liberties and exposures. The allocation of rights and duties to different agents constitutes direct interdependencies beyond price-determined and arm’s length “market” relations. Consequently, it is social institutions which determine these allocations, bargaining processes, *relative prices*, and the distribution of income, wealth and power. The institutions may be changed in manifold ways to better serve future negotiations of interest conflicts.

Resulting prices and distributions must be transparent and *reasonable* for the different social groups. Thus, the structure of values that may minimise the level of conflict has the character of a collective good. These, in turn, can be generated only through all agents taking their *common future* into account (futurity). Effective collective action, not at least public action, is needed to *shape the institutional conditions* for the generation of an overall reasonable structure of values.

This is the idea behind the *negotiated economy* concept, which is connected to an institutional reform policy agenda (Commons 1934). It is a participative policy conception. At its basis are transactions involving direct man-to-man relations.

As *institutions* determine the allocation of rights and duties, they are restrictions as well as *enablers* of individual action. They restrict, and free, individual action. Without institutions, action could easily be blocked, misled, reduced or distracted in a complex, turbulent and highly uncertain environment.

Obviously, governance is a non-trivial issue that requires “processuality”, futurity, institutionalisation and continuous institutional reform in order to solve complex collective problems with mixed interests, through societal coordination and coherence.

So, for instance, the institutionalist analysis of corporate governance that was established by Berle and Means in the early thirties involved the relative power of organisation both within and outside of contracts, and inside and outside of hierarchy (for example, vis-à-vis households and the general public), and its distributional effects (Berle, Means 1932).

Other institutional economists like Polanyi (1957) and Boulding (1970) have dealt with the real-world *diversity of coordination mechanisms* and their hybrids that realise relative efficacies in evolving processes. The processes involve collective learning of forms

of coordination in complex environments, where the common future is important to the agents and where the emergence of trust, commitment and institutional behaviour are supportive.

This institutional analysis of governance is far from assuming any kind of “optimality”, “efficiency” or “teleology” of interactions and processes. Rather, it is about ubiquitous potential *blockage of action* and of forms of “wrong”, “outmoded”, or “petrified” forms of coordination where institutions that once helped coordinating agents have become “sclerotic” and rigid (institutional hysteresis), prematurely *age*, and coordinated behaviours become *locked-in* (Arthur et al. 1985, David 1985, Schoenig 2001:313-330, Javary 2001). Whether and in which ways this may happen is analysed using path dependence. Blocked or locked-in processes call for *continuing examination of institutionalised governance to renew collective action capacity* in order to leave an “old” path and a locked-in situation when their efficacy has decreased to non-acceptable levels.

### **Real World Governance Problems Today: Interdependence, Complexity, Uncertainty, and Networks**

The economy is a socio-economy in the sense that its agents are directly interdependent in manifold ways. Particularly, the modern economy has assumed a more *de-regulated*, *net-based*, and *clustered* character through continuing intensification of *direct interdependencies*, where the outcome for A directly depends on the behaviour of B, and vice versa.

Direct interdependencies are genuinely complex, and complex situations, in turn, cause non-trivial coordination problems. They involve *direct interactions* of agents, which can neither be effectively conceptualised nor performed by the ideal “market”. *Prices* do not account for direct

interdependencies and, therefore, are incapable of generating and diffusing *information* and the formation of future *expectations* required to effectively coordinate agents. They cannot stimulate the collective action capacity required in complex situations.

"Neo-liberal" globalisation is a political and administrative project, regulated by highly selective strategies of de-regulation and empowerment of capital and corporate concerns (Elsner 2003). The global layer of exclusive activities has become dis-embedded from the social institutions that used to exist in the nation-states and in national, regional, and local cultures. The "neo-liberal" construction of the global space has deliberately reduced collective action and social control capacities. It has, thus, become a system of *social fragmentation* (in addition to *spatial fragmentation*) and can be called a system in "*institutional disequilibrium*" (Padoan 2001). Being "under-socialized", it does not provide enough "structure". This is true even for the most powerful individual corporate agents. Hence, the corporate economy, being insufficiently co-ordinated, faces increased *uncertainty* and turbulence. As a result, instability and transaction costs (especially, information costs) have increased. Consequently, powerful corporate organizations find it necessary to increase their *power* even more to keep control over their socio-economic environment and, thus, the global system has increasingly become a power-based, and re-distributive, mechanism, generating ubiquitous negative external effects on third parties, the social commons and the natural environment, rather than a mechanism for comprehensive, sustainable and deliberate innovation and capacity enhancement. Increased uncertainty, instability and turbulence generally have assumed levels that are counterproductive for problem-solving.

Note that we are discussing *true uncertainty* which is "strategic" in the sense that, with ever more fragmentation, the individual agent can neither know at the outset nor calculate with a certain probability, the strategic choices of other agents (Dequech 2001:919f.).

Globalisation has also increased the momentum of vertical disintegration in value-added chains and the redefinition of the boundaries of corporate organization in an effort to reduce labour costs and to control an enhanced labour force world-wide. Value-added chains not only have been spatially fragmented by selecting labour and suppliers at optimal locations around the globe, they have also become *functionally fragmented*.

Functional fragmentation involves securing technological compatibility and complementarity in the chain in an effort to create coordination and *quasi-reintegration* of production and innovation (on a fragmented basis). Again, it has involved individualistic, power-led solutions on a hierarchical basis, e.g., the transnational corporation and its centralized hub&spoke supplier networks.

In addition, the "new" economy is characterised by *net-based technologies*. As such, no decision can be made without a technical dimension, and no technically influenced decision can be made without technical complementarity and compatibility with others. In this way, each decision, piece of information, and innovation possesses positive or negative *externalities*. Every decision is relevant for effective communication and interaction among agents.

This is but one aspect of the fact that information today increasingly displays the features of a collective good. Information has always been characterized by *non-rivalry* in consumption. Regardless of the fact that generating and exploiting asymmetric information is a dominant and "rational" opportunistic strategy in an individualist

environment, *joint use* (joint consumption) of information is welfare-enhancing and increasingly becomes a basic necessity for social coordination. It is well known in economic theory that the total societal benefit of information, as with collective goods in general, increases with the number of its users. Basic information, thus, is *systemic* - and it is generated collectively from billions of acts of behaviour and learning. Against this background, production and innovation have become systemic as well.

Digital microelectronic technologies have added another characteristic to the collective-good property of information: the (re-)production of most information takes place at *near-to-zero marginal costs*. Further, microelectronic information has virtually become subject to *non-exclusion*, rendering information a full-fledged collective good (Gallaway, Kinnear 2002).

Finally, information and technological knowledge are increasingly user- and context-specific and tacit, and must be developed and learned in a dense, common interactive process.

With accelerating innovation and competing (initially, non-standardized) technologies, uncertain, reluctant and passive, or even completely blocked agents have become an ubiquitous latent feature of the economy (Tirole 1995:ch10.6). The introduction of color TV, video-systems, high-definition TV and computer operating systems are examples from the recent industrial history that demonstrate the ubiquity of latent collective blockages and impeded dissemination of innovation.

It has become more difficult under these circumstances to collect profit in the conventionally commercial way, i.e. through "markets". The recent political and administrative efforts to secure and increase profits through *ever more protected "intellectual property rights"*, in turn,

endanger a continued process of rapid generation and diffusion of new information, knowledge, and cultural material. This agrees with the artificial "construction of scarcity" of information which could easily be provided as a public good and largely be available for free. The enforced power structure, thus, "is increasingly at odds with technological reality" (Gallaway & Kinnear 2002:446).

Besides huge global private power-led ("hub&spoke") networks, international private-public bureaucracies have been established to assist the development of technological *standard-setting*, interface definitions and transfer protocols in order to prevent potential blockages from becoming effective (e.g., Weitzel & Westarp 2002).

All production, exchange, and innovation increasingly include the dimension of a collective good or a *social dilemma*. Here, individual agents have to actively *cooperate* (i.e., to give some sacrifice of immediate self-interest) to generate an effective outcome, but at the same time have individualistic incentives not to do so, and even to gain an extra one-shot profit by exploiting others, if these contribute to the collective outcome. This is a complex situation where coordination is non-trivial.

The corporate economy, including SMEs, has developed new spatial forms of organisation such as *local clustering* in order to establish solutions to compensate for the coordination failures of the markets. Here, agents may enter into processes of *collective learning* of correlated behaviour that coordinates them in a non-"market" way and helps them solve the collective dilemma problems in the background. And clusters may be an effective basis for a more consciously developed kind of coordination, i.e. *networks*, normally established by some subset of firms in the cluster, and on the basis of the trust that has emerged (Elsner 2000:13ff.).

## Self-Governing Network Coordination in a Complex Environment?

However, can “*progressive*”, i.e., problem-solving networks spontaneously evolve, and be self-sustaining and self-governing?

Real worlds of collective-goods and social dilemmas are complex with their *multiple relations* among agents (e.g., Delorme 2001). As every decision/action even in any real “market” has to contribute to some *collective framework good*, i.e., the (re-)production of the environment of social rules (Callon 1998, MacEwan 2000:ch4), this also reflects the fact that the economy inevitably is a socio-economy and that production, exchange and innovation have a collective and dilemma-prone dimension.

Effective action becomes feasible only by way of *complexity reduction*. Decreasing the number of potential multiple relations down to some effective coordinated way of behaviour is feasible only through collectively *learned institutions* of cooperation.

There are many approaches and models to formalize cultural-evolutionary processes which employ mechanisms of “selection”, “crossing”, “mutation” and individual adaptation through learning (from one’s own experience, through imitation, etc.). They formally show that cultural evolution in dilemma-prone settings may result in the emergence of an institution of cooperation, where reciprocal cooperation may be self-sustaining, specifically through the built-in sanction mechanism (Axelrod 1984, Hirshleifer 1997, Dixit 2001, Elsnar 2004).

The behaviour which results *habitually* excludes or restricts the strive for short-run maximization, i.e., a social institution of cooperation emerges in spite of continuing incentives to defect. Individuals, then, can reasonably be expected to *act effectively*, i.e., to manage the now reduced level of

uncertainty. In this way, they become capable and inclined to innovate, that is, to develop more comprehensive and continuous solutions through future-bound collective-action capacity.

## “Network Failure”, and Network Lifecycles

Networks can be viewed as real-world forms of such emergent cooperation. *Progressive* networks are structures and governance regimes that solve problems and are innovative in a wide sense, but do not generate and protect invidious power.

However, the reality of power-centered de-regulated “market” economies imply that networks become dominated by powerful corporate agents. Being private solutions, unregulated networks, in the reality of power-based economies, display tendencies towards *exclusion and collusion*, and, thus, also may hamper comprehensive and sustainable innovation (e.g., the attack of the *Microsoft-Intel* “Trusted Computing Platform Alliance” (TCPA) on open source networks, namely Linux. ).

And even highly innovative networks may petrify and become locked-in forms of coordination in the course of their *life-cycle*. Therefore, to make an operational distinction between progressive and regressive networks one may also refer to a set of properties that define the position of the corporate agents affected in the life cycle of their products, technologies, industries and regions.

## “Good” Network Governance

Progressive networks have inspired, with their structures and governance regimes, contentions about the possibility of self-governing cooperation.

One form of progressive network is what we call the *Linux paradigm*. It is based upon a radical *open source* strategy. Its structure is largely characterized by decentralization,



where hubs do not exert much power, but, rather, assume the role of organizers and moderators (Cohendet et al. 2001, McKelvey 2001, Raymond 2001). This form of network is largely public and highly communicative, nearly anarchic, and is one of the biggest success stories of the “new” economy. Linux, itself, possesses unprecedented and sustainable high speed and high quality of innovation, exceeding that of the system built by one of the most powerful hierarchical structures, Microsoft, i.e., the MS-DOS/Windows operating system.

Interestingly, a core finding of “hackerdom” is that structures of low power and *flat hierarchy* and governance regimes, intended to open information flows and *non-exclusion*, are network properties that favour cultures of effective learning of cooperation and, subsequently, enhance the speed and sustainability of innovation in a broad sense (Foray 1998). If the “network equation” holds, ie.—structure + governance = performance—(Elsner 2004) then we may conclude that the principles developed and applied in this case may be highly relevant as a model of sustainingly innovative networks.

“Good governance” principles and rules aim to promote effective collective action and to avoid the restrictive/collusive character of networks, which makes them vulnerable to sharp external changes and premature aging. These principles include informational openness, guaranteed and continuous *entry* and exchange with the environment, parallel and even “*redundant*” *processes* among network participants, the exertion of the *voice* mechanism irrespective of differences of size and power of participants, learned reciprocity, and others (e.g., de Bruijn, ten Heuvelhof 1995, 168ff.; Maggioni 1997, 238-49; Jessop 1997, 103ff.; Elsner 2004). Sustainably effective networks of this kind could well be ineffective in the short-run, especially, for powerful individual agents.

## The Case for Hybrid Governance

A problem that cannot be solved through private rationality in an individualistic culture is the *continuing* existence of the basic *social dilemma*. This is reflected by the fact that the spontaneous evolutionary process may be highly time-consuming and fragile. The more individualistic the culture is, i.e., the stronger the dilemma-structure, the greater the incentive will be to defect, and, especially, to deviate even from an established institution. Both lab experiments and model simulations have illustrated that hundreds, even thousands, of interactions may be necessary to establish cooperation and that, even then, cooperation may be unstable and occasionally collapse because of small external changes or internal dynamics. The “cooperation vs. competition dilemma” (Jessop) remains.

Further, economies of scale and sunk costs of investments in collective learning, building trust and institutionalised cooperation may lead members to close the network in order to maintain high effectiveness at the expense of future flexibility. Therefore, basic dilemmas about “*openness vs. closure*” or “*effectiveness vs. flexibility*” also exist (Jessop 1997:118ff.).

Finally, there is no guarantee that the collective goods are confined to the limits of these networks, even those that are well-governed. The most effective networks generate considerable positive *external effects* not only among their members but also beyond their limits. And the collective goods relevant here normally are functionally, personally and/or spatially *more far-reaching* than the boundaries of any private-agents networks.

It seems necessary, therefore, to introduce a more comprehensive and deliberate supra-individual(istic) rationality into spontaneous evolutionary processes, and even into “well-governed” networks. Specifically, a *public-policy framework* is needed either to initiate

(i.e., de-block, un-lock) or to accelerate and stabilize the institutionalisation of cooperation. Generally speaking, the societal character of any production and innovation requires an integration even of "well-governed" networks in a larger, i.e., public environment (Maggioni 1997, Elsner 2000:435ff).

Social problem-solving can be promoted by *gradually weakening the social dilemma* structure and, in this way, supports a more cooperative behaviour. This allows for a leaner policy approach which already proved to be useful in fields of industrial policy and regional and local development. Relatively small rewards for cooperation may be effective here and define a 'leaner' policy. And it could be demonstrated that with gradual relative changes in the incentive structure or in futurity, cooperation is more likely to emerge and increase speed and stability (Elsner 2001).

A leaner policy approach constitutes an increasingly established form of governance which of course needs to be managed carefully. Its design includes the definition of aims and the use of (pecuniary and non-pecuniary) promises and rewards, threats and punishments (de Bruijn & ten Heuvelhof 1995:173ff; Elsner 2001:76ff).

Additionally one may increase the "discount parameter" by increasing the probability for the agents to meet again. As Axelrod (1984) already has pointed out, the public agent can increase the importance of future interaction, for instance, through more frequent meetings, dividing projects into several sub-interactions, connecting different projects, etc. so that the same agents will meet in different arenas and become more aware of their interdependence and common future.

Thus, a leaner policy becomes feasible because the cooperation/network mechanism permits a *clearer allocation of the relative*

*interests*, or benefits, as well as of the relative responsibilities, or costs, of the private and public agents. The fuzzy "public-private partnerships" in fashion today, in contrast, lack clear designation of responsibility and run the risk of "privatising politics" or "statization" (Jessop) of the private, though collective, sphere.

Obviously, there is opportunity for the public agent to deliberately *shape the conditions of private interaction* to promote collective learning and institutionalisation of cooperation, that is, to shape the private governance. Thus, this policy approach works by affecting the interaction process of the private agents (Amin, Hausner 1997:18ff). Operational policy conceptions have already appeared for this approach (Lindberg & Campbell 1991; Mizrahi 1998; Yu 2000; Elsner 2001).

### **Meritorisation**

We assume that the potential outcome of the private interaction process can be related to a policy objective in such a way that it is subject to *social valuation* or "meritorisation". The private agents are assumed to be capable of collective production of a "good" that has a potential public value in addition to its private values.

The *merit good* concept been developed into one that is substantiated on the basis of "community preferences" that have evolved from processes of interaction outside the "market" (Musgrave 1987:452). This implies an evaluation of the "market" outcome using a form of social valuation which is broader than, independent of, and superior to the "market".

For our purpose we will define a merit good as one which was originally a collective good but can basically be produced by the spontaneous interaction process described (i.e., a "private good"). This is evaluated with respect to its quantity, quality, relative price,

and the probability, speed and stability of providing it through private interaction.

Specifically, the conception of the negotiated economy has been developed to emphasize the "market" must be embedded in a wider socio-political process (above and, e.g., Commons 1934:612ff,649ff, Ramstad 1991, Nielsen 1992, Jessop 1997:113ff.). We will assume here the existence of an economic policy agent who is legitimised through a process of participatory democratic decision-making. In this decision-making process, public policy objectives can be created which provide the criteria for "meritorisation".

Other branches of hybrid governance approaches view the state as an endogenous factor in a "second-order public good" game-theoretic argument, hence extending the Folk Theorem approach (e.g., Hirshleifer 1997, 500f.).

### **Potential and Limitations of Governance Regimes**

A "hybrid" system of coordination, a "*New Deal*" for enhanced collective-action competence, with well-defined "good" (self-)governance of well-structured cooperative network-arrangements together with a new public policy approach has been outlined here. The policy approach relates specific policy measures to the private interaction system. It also permits the combination of strengths, rather than weaknesses, through a clear-cut allocation of responsibilities and benefits of private and public agents. As such, it is specified through a general interactive and institutionally oriented governance.

The conception of governance is relatively unexplored vis-à-vis the traditional political, state and democracy model that is constituted by national sovereignty, free, equal and secret elections, majority rules etc. Can any governance system provide similar formal legitimacy and collective responsibility

compared to that model? Is governance a "political" conception in this sense? Can it become one? And should it become one? Presently, it seems to be capable of preparing, rather than substituting, official political decisions.

The conception of "interactive policy" clearly distinguishes between private coordination regimes, namely, "well-governed" networks, and the official public realm and state policy arena, however participative and transparently negotiated.

Nevertheless, "governance" has become a central notion of any *socio-economics*. It has the potential to deal with *complex relations* among different and diverse agents who may act, each at different portions, in different environments and allocation mechanisms, including "markets".

Governance suggests the vision of "*re-embedding*" (Ruggie 1997), i.e., the understanding that "thin" and lean coordination forms can, in a complex world, not be "pure" ones. Inclusive and participatory coordination forms "would help to improve the chance of a sustainable outcome by associating all the relevant actors" (Gbikpi & Grote 2002:18). Its potential, thus, includes high requirements, and high legitimacy, both on its *input* and *output* sides.

Finally, governance points to "*mid-sized*" *platforms*, such as "mid-size" groups, sectors, clusters, networks and regions, as the arenas where complex interactions and coordination problems can be solved and (coordinated) action capacity be gained. It thus also is a cornerstone in what is to become a new, interactive, *meso-economics* (Elsner 2000:440ff).

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## Governance, Institutions and Collective Action

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### **Introduction**

The state capacity in steering economic processes seems to have declined due to the impact of globalisation. This situation is associated with an evolution of institutional constellations that transcend the hierarchical separation of states and markets through the establishment of hybrid forms of policy-making, basically resembling the organisational pattern of networks. Accordingly, in the analysis of public policy, a tendency prevails that replaces the notion of government as an expression of the sovereign authority of the state in regulating the social and economic domain by the notion of governance as an expression of institutional variety in policy making.

This concept of governance is meant to denote aspects of public policy in terms of public governance, thus differing from established aspects of corporate governance, which are usually addressed in the theory of the firm. In this context of public policy, governance denotes the process of designing, formulating and implementing policy goals and instruments in line with the diverse institutional carriers of these policies, involving agents from the private and public sectors. Yet in addition to the reconsideration of government behaviour and organisation as determinants of state capacity in policy-making, both formal institutions like legal norms and rules as well as informal institutions like conventions and cultural traditions are taken to the fore.

Due to that reconsideration of the institutional underpinnings of government activities in general, and public policy in particular, the matter of policy reform in transition and development countries plays a

crucial role in debates on public governance. Indeed, the role of governance in economic development constitutes a major analytical topic that shapes the policy agenda of international development organisations like the World Bank, paralleled by the development agencies of industrialising and industrialise countries alike. What comes to the fore at this point is the need for examining the institutional underpinnings of economic development in the setting of globalisation with all of their historically conditioned country-specific features.

These characteristics underline the comprehensive theoretical implications of the notion of governance, which are primarily related to discussions on the analytical orientation of the new institutional economics, involving various strands of theorising on public policy that range from public choice theory to evolutionary political economy. Yet all of these strands of thought share common ground in the concern with the diverse institutional constellations of policy-making. The increasing complexity of these constellations, transcending the conceptual dichotomy of states and markets, then contributes decisively to the outstanding role of the notion of governance for an analysis of those institutional processes that shape the making of public policy in theory and practice.

### **Beyond the Dichotomy of States and Markets**

The historical evolution of capitalist market economies is closely related with the emergence of the modern state as a decisive factor in shaping the institutional order of the market process. The related domains of public and private affairs exhibit a historically variable relationship that reflects distinct patterns of an institutional interdependence between states and markets. These shifting economic borders of the state range from the



provision of minimal public services in support of the self-organised market process to an array of extensive interventions that should inherently contribute to centralist planning modes of regulating the market (Helm 1989). This viewpoint implies that the capacity of the modern state in regulating public policy affairs, based on its endowment with a consistent framework of legal rules and a rational bureaucracy for its administration and enforcement, is itself subject to historically conditioned institutional forms that involve specific manifestations of governance.

In the neoclassical approach, to begin with, theorising on economic policy has commonly proceeded with a market-oriented perspective. It highlights firms and households as optimising actors in the market process, while it perceives the state as an exogenous factor. The corresponding rationale of economic policy is derived from market failures in the promotion of a Pareto efficient allocation, related to the matter of externalities, natural monopoly, and public goods that has been typically explored in the framework of Walrasian general equilibrium models. While economic policy is dealt with as a residual category of the market process, it is fair to maintain that neoclassical economic theory has typically approached the state as an analytical “black box”, that is, as an economic datum (Dixit 1996).

This assessment is of course most relevant for the domain of welfare economics with its concern for a rigorous analysis of the welfare implications of market interventions. Its focus on allocative efficiency and distributive justice has informed the normative conclusions of the theory of economic policy that evolves from neoclassical marginalism, as it relates arguments on market failure with problems of accounting for social welfare functions. Yet despite the policy-related concerns of welfare economics, its

argumentation lacks from institutional specificity that would actually account for the steering capacity of the state in the context of collective action. Thus, in that line of reasoning, the delineation of private and public spheres of economic activity seems to be as unproblematic as the distinction of private and public goods, with the latter perceived as a primary domain of supply through government agencies.

The corresponding problem of dealing with the institutional aspects of government activity concerning public policy, however, applies not only to the Keynesian advocacy of market stabilisation by government intervention, but also to the Hayekian counter-positions on the market process as a spontaneous order. These have persistently shaped the discourse on the relationship between states and markets, outlining the conceptual terrain of the theory of economic policy. Yet both of these distinct perspectives do not allow for generalised efforts in demarcating the terrain of government activity in economic affairs, for, apart from the matter of historical variability, theory itself is bound to value-judgements in its account of the failure of both markets and governments.

However, as the notion of governance indicates, even this differentiation is in itself most problematic. Indeed, associating globalisation with an increasing variety of institutional forms in capitalist market economies that transcend the notion of a simple hollowing out of the state, the changing economic role of the state together with the dynamism of collective action provide a crucial domain for further analytical efforts. In the domain of economic theory, in particular, these efforts are most rigorously pursued by the various approaches to the economics of institutions, covering a far-reaching area that ranges from public choice theory via economic sociology to



evolutionary political economy. Yet this need for a reappraisal of institutional aspects is quite in agreement with more general trends in recent theorising within the social sciences, aiming to bring institutions back in to discussions on the economic role of the state (Weiss 2003).

In this analytical context, the notion of governance takes centre stage as a device for exploring the institutional foundations of public policy. Still, due to the comprehensiveness of the issues under consideration, as well as due to the diversity of the involved theoretical perspectives, a consensus among economists and other social scientists on a commonly shared definition of governance is still missing. Nonetheless, even in critical terms, common ground for approaching the subject is provided by discussions on governance that have been put forward in the framework of the economics of institutions.

### **Institutions and Governance**

Taking neoclassical methodology as a point of departure, and thus differing from older institutionalist approaches that are closer to current debates in economic sociology, the new institutional economics addresses all the domains of individual decisions in economic systems, ranging from firms and households to bureaucracy, government and the polity. Patterns of monitoring and enforcing exchange relations among economic actors are perceived as governance structures that confront the problem of economising on transaction costs (Furubotn & Richter 1997:2-3). A common motive in these considerations is provided by the problem of coordinating individual decisions and their outcomes. Theorising governance thus requires an elaboration of theoretical concerns with the institutional determinants of economic processes that are associated with the cooperation of diverse actors.

The theory of the firm and corresponding aspects of economic organisation have provided micro-analytical starting points for related efforts, paralleled by the matter of public governance, as the capacity of government in implementing specific policies is closely related with problems of governability that point to the coordination of diverse interests and strategies in collective action. In addition to like-minded discussions on governance in terms of government behaviour and organisation, however, which are related to the so-called good governance imperative in policy reform that is promoted by the World Bank and other development-related organisations, the wider societal context is also taken to the fore. This most recent reconsideration of the embeddedness of governance processes in the diverse institutional segments of civil society then points to the impact of institutional networks as coordination mechanisms that transcend the dichotomy of markets and hierarchies.

The matter of corporate governance constitutes the corner stone of the transaction cost approach in the theory of the firm and related arguments on economic organisation, which are associated with Oliver E. Williamson's contributions. In that particular line of reasoning, governance is defined in terms of a microperspective on firm and market modes of contract and organisation, which are perceived as variable arrangements within an established institutional environment (Williamson 1996:322-8). Specifically, according to Williamson's transaction cost perspective, forms of governance in the continuum of hierarchies and markets denote the institutional means for accomplishing order in terms of a mitigation of hazards in a setting that is characterised by potential conflict among self-interested actors. Credible commitment as a means for dealing with the opportunistic behaviour of individual actors is addressed as a decisive

condition for establishing effective modes of governance.

Approaching the theory of economic policy in terms of these institutional aspects, however, requires that the related notion of public governance, as discussed primarily with regard to the modernisation of public administration, is distinguished from Williamson's transaction cost theory of corporate governance and industrial organisation. This holds especially with regard to the underlying institutional aspects of incentive systems and property rights as characteristics of a governance structure (Dethier 1999:7-8). Indeed, in the domain of public governance, which is most relevant for the matter of public policy, the coordination problems that are to be dealt with do not primarily occur among interacting firms, but include multiple actors from the public and private sector with a focus on the state apparatus in its entirety. This underlines the appropriateness of a refined definition of governance capacity as "the ability to coordinate the aggregation of diverging interests and thus promote policy that can be credibly taken to represent the public interest" (Frischtak 1994:vii.). The underlying reconsideration of tensions between private and public interests then constitutes a major analytical challenge.

Corresponding discussions in the economics of institutions assess the economic role of the state in terms of its functions in defining and enforcing economic rules. As highlighted in the public choice approach, the state provides a terrain for self-interested actors, who persistently compete for scarce resources as vote-maximising politicians in government or as budget-maximising bureaucrats in public administration (Frey 1983). Democratic government may be viewed as a set of relational contracts between a sovereign population and its elected representatives, modelled as a

principal-agent-relation in public affairs. Problems of monitoring and enforcement that arise from the transfer of political property rights are to be solved through constitutional incentives and control mechanisms (Furubotn & Richter 1997).

From a broader developmental viewpoint, property rights and transaction costs serve as the institutional basis for economic performance, as emphasised in Douglass North's influential definition of institutions as "rules of the game in a society" in coping with economic as well as political exchange, involving formal and informal constraints as well as enforcement mechanisms (North 1990:3). In this context, the relationship between state and private sector is marked by a dilemma of governance, namely the need for controlling the coercive power of the state. The rationale of political institutions may be associated with the creation of a governance structure that promotes the self-restraint of the state. Consequently, credible commitment in political exchange resemble institutionalised *ex ante* agreements about cooperation, involving legal rules and cultural norms (North 1990:50). The corresponding question of the adaptive efficiency of the governance structure of a political-economic system becomes a decisive factor in economic development, shaped by the path dependence of cultural evolution (North 2005).

In rejection of a mechanistic account of decision-making and enforcement procedures in economic policy, it follows that the behaviour of political and administrative actors resembles an endogenous variable in the institutional framework of the political-economic system, underlining the crucial role of incentives in related coordination processes (Eggertsson 1997). Such a reconsideration points to the matter of governability and the pitfalls of collective action as crucial elements in analysing the institutions of governance. Indeed, the matter

of governability, which is related to the problem of maintaining institutional designs that are fit to promote collective action, may be perceived as the most pressing point of departure for debating governance beyond the confines of government behaviour and organisation. As such, it transcends the sphere of public governance in favour of a more inclusive approach that has the potential to account more sensitively for the institutional context of the diverse governance aspects of public policy.

### **Governability and Collective Action**

In dealing with governability, the notion of government failure complements the concept of market failure that has been prominent with welfare economics, rejecting assumptions of an omniscient and benevolent state. Apart from institutional malfunctions within the administrative apparatus that are usually related with the competition of self-interested policy actors, government failure is also said to result from persistent interest groups activity. This points primarily to procedures of rent seeking, meant as the promotion of policy measures by special interest groups that serve the particular benefit of their members while imposing external costs on the majority of the population. The related types of bargaining procedures among involved agents in the political and economic system then determine the actual supply of collective goods as the decisive manifestation of productive government services (Frey 1983:121-2).

Following the recognition of interest group activity, especially when viewed from a public choice perspective, the autonomy of the state from particular interest groups emerges as an indispensable requirement for promoting the functions of government and public administration. For instance, in James Buchanan's approach to the functions of government in a constitutional framework,

the state needs to be established as an autonomous actor, as it fulfils both a productive function regarding the provision of public goods, like a legal order, and a protective function, which implies the third-party enforcement of contracts (Buchanan 1975:95-6). This need for institutional autonomy becomes even more important with an increase of government activities, for a steady expansion of public budgets may be viewed as a response to interest group interventions. Therefore, institutional crises of government in terms of a declining governability inform related proposals for reform, which suggest the establishment of rule-guided decision-making procedures that aim at promoting an insulation of the polity from interest groups. At this point, the notion of governance is closely related with theories of interest group activity in democratic market societies, involving arguments on pluralism and corporatism as modes of political organisation.

In particular, Mancur Olson's theory of collective action represents a most influential approach to institutional analyses of public policy, providing basic concepts for current theorising on governance. Indeed, Olson's reconsideration of corporatism and pluralism reflects a concern with ungovernability as a loss of steering capacity in the domain of economic policy. According to Olson, the logic of collective action does not follow the pluralist pattern of a symmetrical and spontaneous self-organisation of interest groups. Instead, group size represents a determining factor in the provision of collective goods, related with the incentive-based formation of group-oriented behaviour that reflects a rational pursuit of individual interest. In this context, Olson argues that small interest groups exhibit organisational advantages due to a less costly monitoring of individual free riding on the collective good that is provided by the group, leading to a

persistent organisational dominance of particular interests over the presumed general interests of society at large.

In application of this argument to the comparative economic performance of nations, Olson identifies the impact of small interest groups as the decisive source of economy-wide inefficiencies that are associated with ill-conceived economic policies, favouring divisive strategies of redistribution over growth-oriented perspectives (Olson 1982). The decline in the steering capacity of the state then results from the impact of particular interest groups that decompose the coherence of policy design and implementation due to an increasing divisiveness in political bargaining, leading to institutional sclerosis. Under conditions of political stability, perceived as a requirement for the accumulation of organisational capacities in collective action, the expansion of interest groups promotes the establishment of distributional coalitions, which induce an expansion of government interventions, while institutional sclerosis prevails.

However, Olson's claim that the economy-wide welfare loss from rent seeking will rise with the organisational degree of special interests does not deny that those interest group organisations, which encompass a substantial fraction of the population or its resources, may actually even promote economic growth, as they could find such an orientation to be in their own interest. Government then resembles the most encompassing organisation, commanding a policy capacity that is assessed with regard to its relative strength in comparison with less encompassing special interest groups. Consequently, according to Olson, policy reform requires either strengthening government or weakening the narrow types of special interest groups. Therefore, reflecting institutional problems of governability and collective action as a basic concern of

Olson's theorising, differences in the institutional setting as well as in the related orientation of economic policies are identified as the major cause of diverging growth patterns and development trajectories among countries (Olson 1996).

In addition to problems with the historical and empirical corroboration of these arguments, a common criticism of Olson's theory takes issue with its specific behavioural microfoundations, primarily with the thesis that rational actors would systematically tend to free ride and thus refuse contributing to the production of a collective good. It is argued that Olson's underlying behavioural assumptions, such as individual opportunism, almost necessarily lead to an almost exclusive interpretation of interest group activity in terms of rent seeking. In contrast to that, competing interest groups may also promote efforts in the self-regulation and cooperation of economic actors, based on relational factors like knowledge flows and trust, as illustrated historically by industrial associations that contribute to the provision of collective goods like education and training (Unger & van Waarden 1997).

Yet another serious problem with Olson's interest in governance and governability lies in an implicit idealisation of the steering capacity of the modern state. Indeed, Olson's policy conclusions indicate that governments may regain their presumed steering capacity as soon as they are effectively set free from the redistributive influence of intervening small interest groups. Hence, Olson's theory of collective action not only fails to acknowledge enabling aspects of institutional variety in the making of economic policy, but it also ignores the ongoing institutional transformation of the state that marks the specificity of governance in the current process of economic and political globalisation (Messner 1997:90-1).

Accounting for that matter points to the need for a further reconsideration of the institutional processes that actually shape the governance capacity of the state. Indeed, arising from this criticism of Olson's arguments, transcending the more narrow concern with government authority then implies an appraisal of the institutional embeddedness of governance.

### **From Government to Governance**

Approaching governance as an institutional process points to those particular strands of political economy, which maintain that theorising on economic policy needs to address the actually existing variety of institutional forms in the coordination of economic actors apart from the seemingly ubiquitous market mechanism (Chang 2002). Beyond the dichotomy of states and markets, institutional variety is thus perceived as a constitutive feature of economic policy. Public goods then resemble multi-actor products, as various actors apart from the state are involved in coordinating their provision, in particular coming from the private business sector and civil society (Kaul 2001). Indeed, as the dichotomy of private, market-based and public, state-based resources rarely holds, a mixture of these pure types of goods represents the usual case in modern economies. In accordance with that position, both the setting of formal collective choice arenas such as legislatures, as well as informal collective choice arenas, which are commonly represented by private associations, need to be taken into account when exploring the institutional terrain of governance (Ostrom 1990:53-4).

Grasping that perspective, a suitable definition of governance that transcends the more narrow confines of both corporate governance and public governance as distinct modes of coordination has been pointed out as follows: "Governance is the capacity of a

country's institutional matrix (in which individual actors, firms, social groups, civic organization and policy makers interact with each other) to implement and enforce public policies and to improve private-sector coordination" (Ahrens 2002:128n). This notion of governance is well designed to address those institutional aspects that tend to share the concern with governability, as pointed out in Olson's theory of collective action, while allowing for a reconsideration of institutional variety and its implications for an assessment of state capacity.

In particular, contrasting the notion of government with its hierarchical connotations, governance may be associated with reflexive self-organisation and rule-based, decentral steering capacities in the policy domain. The concept of the state as the central agency of political steering, implied both in pluralist and corporatist approaches, is abandoned in favour of a reconsideration of the blurring institutional boundaries between the public and the private sector. In a wider sense, the structure of governance highlights the constellation of institutional arrangements, which coordinate the interactions among diverse actors that outline the actual pattern of the governance process. In a more narrow sense, however, pinpointing its impact on public policy, governance denotes institutional structures and processes that mark the formulation and implementation of policy goals and instruments, involving the coordination of actors from the public and private sectors. Governance thus resembles a collective good, provided by a variety of formal and informal institutional carriers, involving the state, which is by itself to be viewed as a multifaceted organisation that involves formal and informal arrangements (McGinnis 1999).

Apart from aspects like the structure and performance of incentive mechanisms in public administration, the matter of

contextual embeddedness plays a major role for the structuration of governance processes with their diverse rules, norms and conventions. Accordingly, in the course of an increasing complexity of institutional forms in the socio-economic domain, the need for both horizontal and vertical coordination among policy actors highlights policy-related efforts in communication, coordination and integration. The state then becomes an institutional player in an extended field of diverse governance modes that involve intermediary institutions with their capability for self-organisation (Messner 1997:133-4). This perception of governance as an expression of a shifting role of the state implies a reconsideration of that “third sector” of civil society institutions that is addressed as a highly relevant factor in corresponding efforts of formulating and implementing public policies.

The appraisal of the institutional embeddedness of governance structures and processes goes well beyond the notion of public governance as a manifestation of government behaviour and administrative efficiency, not only due to the fact that it involves formal and informal institutions, but also because of the concern with the relations between different levels of government and administration, addressed in terms of multi-level governance, as well as between the state and the wider spheres of society at large. Yet this perspective amounts to the recognition of relational modes of governance that are most prominently associated with the notion of institutional networks.

### **Institutions and Governance Failure**

References to the moderating, monitoring and mediating function of the state, meant to prevent the kind of institutional particularism that is often identified as a major source of losses in the steering capacity of the state, usually point to the constitutive role of

institutional networks in the organisational pattern of governance process. In this setting, the matter of institutional networks highlights the inherent advantages and limits of governance both theoretically and empirically, allowing for a perception of governance as a most crucial mode of coordination in the contemporary type of “network society” (Messner 1997).

Networks modes of coordination differ from horizontally coordinated markets as well as from vertically coordinated hierarchies. Their actors are loosely joined in long-term relationships that coincide with the attributes of reciprocity and trust, ensuring cooperation in repeated exchange procedures. Thus, they combine the exchange rationale of markets with the cooperative rationale of hierarchical organisations (Powell 1990). This reading of institutional networks as a specific mode of governing the interaction of diverse actors resembles the thesis that norms of reciprocity and trust facilitate solutions for the appropriation of common-pool resources that differ markedly from those solutions that favour an exclusive role of private property or government interventions (Ostrom 1990:211-2).

Concerning public policy, the role of networks in the specific phases of policy-making involves problem identification and development of solution-oriented approaches, contributions to the definition of distinct policies and their implementation, as well as evaluation and correction of these policies (Messner, 1997:298-9). A pattern of horizontal network structures, marked by weak ties among the involved actors, then contributes to the comparative institutional advantage of adaptive flexibility in a turbulent socio-economic environment. Still, network failure may be due to coordination problems in competition and cooperation, disturbing trust and reciprocity. Moreover, cognitive blockades due to a homogenisation

of expectations may lead to an institutional sclerosis that obstructs the capability for innovation. This points to the problem of closure in networks, yet it is also meant to underline the relevance of governance attributes like responsibility, transparency and efficiency (Jessop 1999).

However, in the case of policy networks as components in the institutional architecture of governance mechanisms, the establishment of general rules may promote the evolution of sustainable negotiation systems that may promote communicative efforts in policy making (Marin and Mayntz 1991). An assessment of these specific institutional constellations implies a reconsideration of the strategic relationship among the involved actors in a setting of reciprocal interdependence that characterises the distinct pattern of network-based governance regimes (Scharpf 1991).

From these considerations follows that comprehensive planning efforts in terms of a constructivist design of a complete system of governance mechanisms in the domain of economic policy remain out of reach. Still, with regard to the pattern of state-society-synergies that may characterise governance processes, the impact of socio-cultural endowments that are difficult to change in the short run, as reflected by factors like prior stocks of social capital and the quality of government institutions, is to be confronted with possibilities of a constructability of synergetic relations by the means of institutional entrepreneurship. The latter aspect points at the role of government and administration in promoting the scaling-up of local social capital to an aggregate level of rule-guided interactions (Evans 1996:1124-7).

Allowing for the evolutionary character of institutional change, then, changes in a governance structure that may be perceived as an institutional matrix of relational contracts resemble procedures of experimentation,

discovery and adaptation (Ahrens 2002:14-5). Accordingly, there exists no well defined optimum in the adaptive solution to the problems of governance. Thus, the need for requisite variety and plurality of governance mechanisms prevails. Reflexivity and learning constitute core capabilities in these processes, based on communicative interaction and the cognitive convergence of the particular strategies that are pursued by involved actors (Jessop 1999:9-10). Choices on the selection of policy goals and instruments, which are inherently shaped by specific modes of communication, may become subject to path dependence, thus contradicting rigorous notions of efficiency in policy choices.

From the viewpoint of the economics of institutions, this position corresponds with the argument that asymmetric information causes a type of government failure that is rooted in the dynamic character of economic policy as an institutional process with diverse actors. While governments, as enforcers of contracts, are unable to make credible commitments, the impact of uncertainty and imperfect information may impede the dynamism of bargaining processes. Governance then promotes Pareto improvements by allowing for credible commitments and informational transparency as crucial requirements for bargaining processes among actors who are involved in the making of economic policy (Stiglitz 1998).

Following that line of reasoning, it becomes necessary to examine whether governance structures provide devices, which promote changes in the information environment of economic actors, supporting learning processes in accordance with selected policy targets (Eggertsson 1997:1197-8). Indeed, highlighting the matter of knowledge and learning, the perception of governance as an institutional process points both to the possibilities and limits of policy

making in the complex political-economic systems that mark the contemporary terrain of public policy.

### **Policy Implications**

In conclusion, the notion of governance combines scepticism regarding the steering capacity of the state with sensitivity for the coordination problems of collective action and the pitfalls of interest group activity. Corresponding policy conclusions point to the outstanding role of partnerships and complementarities between government and the private sector (Stiglitz 2003). In particular, network-based modes of governance are said to be related with the influence of associations and other interest group organisations, affecting formal as well as informal modes of participation in the making of economic policy, as conditioned by an increasingly fragmented and decentralised state (Messner 1997:150-1).

Indeed, in the context of an increasing institutional complexity that is driven by globalization, the nation-state is transformed into a polycentric system with a distributed capacity for self-steering that coincides with a drive for shared sovereignty in terms of cooperation and integration (Cerny 2000). This aspect points to the role of multi-level governance in a setting of regional integration, to be viewed as a facet of globalisation, as for instance represented by the governance patterns that characterise the European Union. A perception of governance as an institutional process needs to account for that interdependence of diverse policy levels, thus also recognising a possible source of governance failure. For instance, regular problems of multi-level governance may reflect the need for strong supra-local institutions, which may arise in the context of intensified regional policy interaction due to the rent seeking strategies of particular local interest groups.

In debates on state capacity and governance in economic globalisation, then, the position prevails that national governments continue to play a decisive role in the coordination of economic activities, especially regarding the institutional orchestration of a stabilised social consensus (Hirst and Thompson 1997:350-1). In this case even as an enabling force, globalisation is said to create pressures for cooperative responses to problems of collective action that are associated with the structuration of domestic institutions (Weiss 2003:18-9). Thus, the nation-state remains a crucial terrain for confronting the challenges of economic development and structural change by means of adequate governance procedures in public policy.

This position also shapes the domain of policy strategies in support of poverty reduction, as promoted by the World Bank and other Bretton Wood institutions that constitute the institutional framework for development assistance and cooperation. In this context, governance is basically perceived as a cooperative steering approach that should allow for participation, transparency, efficiency and responsibility, quite in accordance with rule-guided procedures in a well-established constitutional framework (Grindle 1997). More specifically, the programmatic notion of “good governance” has become a component of the World Bank’s strategic orientation, as it concerns the efficient management of a country’s public resources, addressing constitutional aspects in establishing the rule of law. In related analyses of economic development and transformation, the notion of “good governance” shapes discussions on reform opportunities in government and administration (World Bank 2000).

This orientation is related with the experiences of structural adjustment programs in the 1980s, which had been pursued in



terms of a liberalisation and deregulation of the economic sphere. Above all, the impact of the institutional order on economic performance has informed the concern with governance as a policy device, confronting institutional deficits in a country's governance capacity as a developmental hindrance. In particular, the World Bank report on the problems of implementing structural adjustment programs in Sub-Sahara Africa, published in 1989, may be identified as the point of departure for the policy-related debate on the role of governance in economic development (World Bank 1989). In this document, the World Bank comes up with the diagnosis of the persistence of African underdevelopment as a manifestation of a persistent "crisis of governance", basically attributed to the performance of government and administration. The institutional context of policy-making is taken to the fore, highlighting mismanagement of the public sector, lacking accountability and an inefficient legal system that promotes corruption and rent seeking. In this context, governance is addressed in terms of "the exercise of political power to manage a nation's affairs" (World Bank 1989:60).

In agreement with that assessment, the World Bank suggests comprehensive governance reforms, emphasising the necessity of establishing the rule of law in all branches of government and administration. Paralleling an independent judiciary, the implementation of rule-guided government behaviour and the transparency of administrative procedures, based on efficient accountability standards, stand out as elements of reform processes. As such, they should become the pillars of "good governance" in the strategic outlook of the World Bank (World Bank 1992). More specifically, this implies an efficiency-enhancing reform of public sector management, involving measures like

privatization, outsourcing, and public-private partnerships with regard to the provision of public goods. The related matter of accountability includes the promotion of fiscal decentralisation and local government, meant to contribute to the informational and procedural transparency of the public sector. However, all of these measures are framed by the persistent need for a reform of the institutional underpinnings of the political-economic system in terms of the rule of law.

Derived from these concerns with policy reform, the World Bank has issued a refined definition of governance, now highlighting "the manner in which power is exercised in the management of a country's economic and social resources for development" (World Bank 1994:XIV). In this context, three distinct areas of governance are identified, namely the political system, the procedures that manifest the authority of the state in its developmental efforts, as well as the capacity of government in designing, formulating and implementing specific policies and measures. Therefore, also with reference to its recent focus on problems of corruption, it is fair to conclude that the World Bank approach to governance tends to underline the dimension of public governance.

However, also the more comprehensive concern with the institutional embeddedness of governance processes in the relationship between the state and civil society has been applied to the policy domain by international development organisations. The United Nations Development Program UNDP, in particular, makes use of such a more encompassing approach to governance (UNDP 1997:9). Indeed, the UNDP views governance as the exercise of political, economic and administrative authority in the management of national affairs, addressing the institutional mechanisms, procedures, and relationships that are involved in the articulation of individual and collective

interests and the solution of conflicts. In this framework, distinct types of governance are taken to the fore that correspond with specific sectors of public policy, including economic governance, political governance, administrative governance, and systemic governance. It is especially the latter aspect, pinpointing the cultural dimension of governance in support of sustainable development, which points to the inherent interdependencies between state, market and civil society.

These considerations underline the analytical advantages of the notion of governance, for it addresses both the formal and informal institutions of any political-economic system. However, with reference to the fundamental role of institutional networks and social capital for the developmental dynamism of all modern societies, the notion of governance also exhibits an even more general analytical value that may gain in significance with the increasing institutional complexity that is stimulated by the process of globalisation.

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 Resource Centre. [www.grc-exchange.org](http://www.grc-exchange.org)  
 Governance. <http://topics.developmentgateway.org/governance>  
 United States Aid.  
[www.usaid.gov/our\\_work/democracy\\_and\\_governance](http://www.usaid.gov/our_work/democracy_and_governance)  
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## Ideology

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### Introduction

We will begin by providing a list of ideologies and then attempting a definition of one of the most contentious of all terms in the English language. It will outline the interesting etymology and evolution of the term, a process that has influenced many later ideologies. Part I will provide a historical outline of the evolution of ideological *categories* and *dichotomies* (left/right, liberal conservative et. al.) in four stages. It will also provide oversimplified but not distorted definitions using two or three key ideas.

Part II will present the main reasons for contesting the standard (since 1789) left-right one-dimensional political spectrum. It will be criticized on logical and historical grounds, then replaced by a Cartesian grid.

Part III examines two contentious issues of relevance to public policy: first, the mostly philosophic debates about the logical implications (if any) of ideology to public policy choices (gay rights, the welfare state, abortion, affirmative action et. al.). The second concerns the more pragmatic issue of whether or not ideology actually does influence the decisions and policies of either political leaders or their followers, whether the latter are voters, party members or citizens in non-democratic states.

Part IV will examine various theses about the ideological foundations of democracy organized around contentious themes concerning “The end of Ideology”, “The end of History” and the distinction between ideals and ideologies. Part V will briefly summarize two of the more interesting theories attempting to explain ideologies: Those of Emmanuel Todd and Hugh Graham.

Three main arguments of this article are that (1) The time-honoured Left/Right

dichotomy is no longer useful for classification purposes although it is still highly useful for polemical purposes in contemporary ideological wars. A more useful distinction is in terms of attitudes to democracy with democracy treated as an ideal not an ideology. The lingering positivist conception that ideologies are immune to logical, rational argument and refutation will itself be refuted.

The basic “uncontestable” list of ideologies is: Liberalism, Conservatism, Socialism, Anarchism, Nationalism and Fascism. Andrew Vincent adds to this list both Feminism and Ecologism. At the outset we should distinguish between the origins of “ideology” and the origins of ideology. Both *could* be said to owe their genesis to the period of the French Revolution. The former, the term itself, unquestionably does, since it was invented by Tracy de Stutt in 1796. The latter, the phenomenon itself, is arguably the invention of this period also. The fifty years after the term was coined saw a curious development in its’ use. It was originally meant to be a word defining a field of scientific study after the analogy of biology, psychology, sociology, geology et al.

In de Stutt’s terminology it meant the study of ideas; development of an empiricist study of the origin of ideas in the Locke/Condillac tradition. It started to acquire both its modern political and also pejorative connotations with Napoleon, a process that culminated in Marx and Engels’ *The German Ideology* (1845). It thus morphed in two radically different ways: first from a psychology to a sociology of ideas and also from the general study of ideas of all types to one specifically focused on political ideas.

The transition from a neutral (or even scientific) to a partly (or often mainly)

pejorative use of “ideology” was due to a very heterogeneous set of thinkers: Bonald, Schopenhauer, Napoleon, Comte, Marx and Dilthey. This entailed a switch from a purely empirical to a primarily anti-empirical meaning. For Marx and post-Marxist social science, ideology is a social, not a philosophical, phenomenon and is usually seen as a “distortion”. But the same is true, as we shall see (e.g. in Ken Minogue), on the opposite side of the ideological spectrum.

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### Contemporary Definitions of “Ideology”

John Plamenatz argues for the following four criteria for an “ism” to qualify as an ideology: It must be held by a group, it must concern matters important to the group, it must be functional and it must justify actions and attitudes characteristic of the group. This has the advantage of distinguishing ideology from both political philosophy and political theory. Thus, if Plato, Hobbes and Machiavelli alone hold their distinct views they are political philosophers not exponents of an ideology. But if they attract a following meeting the above criteria then their ideas become ideological. However as it stands it would also include most of the world’s religions as well.

Ball and Dagger (2003) also offer four desiderata: an ideology “*explains* political phenomena”; it provides “standards of *evaluation*”; (3) it “*orients* its adherents”; and (4) provides “a rudimentary political *program*”. Number (3) requires some brief elaboration: it means that ideologies provide adherents with both an individual and collective identity (e.g. member of a superior race or nation, member of a class fighting oppression or member of a group working for minority rights).

Gordon Graham offers as a definition: “those sets of belief which have or are meant to have wide implications for the conduct of

political life and even...for its complete refashioning.” He offers four desiderata worth comparing with those of Plamenatz: 1. It must be reasonably consistent and coherent; 2. Its claims must be true. 3. It must be applicable in some political context 4. It must appeal to political values shared by those who do not yet subscribe to it.

Graham claims that these factors help make rational debate possible challenging the dogma that “ideological disputes involve irresolvable differences over incompatible principles or values”. He also claims that there is no definitional essence to various ideologies.

Plamenatz’ third criterion fits in with some of Graham’s arguments. The latter requires that an ideology “must give some political guidance”. This is arguably a very good desideratum that will be incorporated into this analysis and will be discussed in section III, with specific examples.

Minogue, in his provocative *The Pure Theory of Ideology*, provides a good example of an anti-leftist definition of ideology that makes it guilty of anti-empirical and other sins. For him, ideology consists of two key axioms, “all evils are caused by an oppressive system” and “truth is a weapon”. He argues that: “for all their differences, ideologists ....share..(a) hostility to modernity”. This entails in turn hostility to “liberalism in politics, individualism in morals and the market in economics”. Therefore ideology is essentially hostile to modernity. Ideology is hence Platonic which means a doctrine of “differential consciousness” resulting in a self-constituted cognitive elite “whose participation on an equal basis with others would be an intellectual absurdity.”

The idea of differential consciousness means that the majority of people unfortunately (not necessarily their own fault) lack the knowledge and expertise to handle complex political questions and it should

therefore be an elite (Plato's "philosopher-king", the vanguard of the proletariat, scientific experts in progressivism or Comptean positivism) who should use their superior knowledge for the interests of the "vulgar herd".

This raises the crucial question: "Is a neutral definition possible?" Before trying to answer this let us note two radically differing types of negative definitions: utopian and conservative. The former claims that ideologies are mere rationalizations for the status quo, the latter that they are unrealistic goals to justify future revolutions.

The definition to be used in this article is based on Ball and Dagger: An ideology is "A fairly coherent and comprehensive set of ideas that explain and evaluate social conditions, help people understand their place in society and provide a program for social and political action". It will be the preferred definition for this article since it seems to be the most neutral and comprehensive as well as the least question begging.

A good definition must distinguish between ideologies on the one hand and both religious and moral theories on the other even though they may incorporate elements of either or both. Most ideologies contain a (putatively) scientific, cognitive component, a moral theory (or at least views about the good and/or just society), a political program and usually a religious foundation and/or one based on a theory of human nature. The "scientific" component can include both natural and social science, where biology is more likely to be the basis than physics or chemistry. It can even be based on a theory of scientific method as in the positivism of Comte or as in Marx and Karl Popper.

An advantage of the above definition is that helps demarcate ideology from political theory, morality and religion while allowing all three to be components of an ideology. How then can we distinguish between an

ideology, a political philosophy and a religion? The following will suffice for this article. A religion (Islam, Buddhism et. al.) concerns itself either with salvation and redemption in the next world (eternal life, nirvana, reincarnation, immortality) or offers an incentive of some kind for moral and spiritual improvement in this life independent of any social or political change or preservation of the status quo. But when it offers or advocates a this-worldly redemption, salvation or jihad then it is an ideology as well as a religion. So Islam can be both. It can concern itself with saving souls for the next world or with drastically altering political and social conditions in the here and now.

Here it must be conceded that from some ideological perspectives even a solely other-worldly religion has ideological functions insofar as it may deaden appeals for improvement in this world by focusing people's attention on the after life. This is how many people take Marx's dictum "Religion is the opiate of the people". It is usually interpreted to mean that, by diverting attention to the next (fictional) world it distracts people from improving or revolutionizing this (the only real) world. Or, to take the opposite extreme, religion can be criticized by a Hobbsean or Nietzschean precisely because it encourages civil war, revolution or a slave morality revolt inhibiting the masters from exercising aristocratic, pagan virtues.

It seems obvious enough that Hinduism qualifies as an ideology as much as a religion and so does Confucianism as well as political Islam. The first has an elaborate metaphysics, epistemology and moral theory with striking similarities to Platonism. As in Platonism, Hinduism (*The Bhagavad Gita* being the prime document) justifies a fairly rigid class or caste hierarchy for this life anyway. Social mobility is deferred until the next reincarnation (or allowed in Plato's case at the



discretion of the guardians).

Plato can be called reasonably the first political philosopher but whether or not he is an ideologist may depend on one's own ideology or definition of "ideology". To some extent Platonism lives on in modern "progressivism" and positivism where scientific experts or the vanguard rather than the people should make the key decisions (as indicated in the discussion about Minogue's "differential consciousness").

Confucianism strikes many as neither a religion or an ideology nor even a philosophy either (since Confucius said little or nothing about metaphysics and epistemology). However it has clearly played the role traditionally played either by established religions and both status quo and reformist/revolutionary ideologies. It is striking that persons as diverse as Max Weber and Chairman Mao thought Confucian thinking has retarded Chinese society from becoming modern earlier.

## Historical Background

### Stage 1

Whereas many might argue that the history of modern ideology begins in 1776 rather than sooner, this is contestable. Admittedly the reasons for the rejected opinion is the reasonable argument that what existed prior to modernity in both east and west were various political philosophies, religions and moral theories. There were debates involving ideological arguments about slavery, serfdom, tolerance, torture, tyranny and monarchy. There certainly were precursors of modern ideologies e.g. Thomas More's *Utopia*, 16<sup>th</sup> century French constitutionalism, antinomianism, peasant revolts, Mercantilism and Medieval Millenialism. But for good reasons the claim that the 17<sup>th</sup> century is when modernity commences is arguably correct due to both the Scientific Revolution and modern

proto-ideologies. It is perhaps no coincidence that 1687, the year of Newton's *Mathematical Principles of Natural Philosophy*, was quickly followed by both the "Glorious Revolution" (1688) and Locke's two treatises on government (1690).

There are three major components in the 17<sup>th</sup> century invention of modern ideology. First the Bacon/Descartes view of science and technology. This involves the idea that the increase of scientific knowledge can be used to benefit the human race. "Knowledge is power" and it can be used to improve our control of nature and hence make mankind better off. The second component is the political philosophies of Hobbes and Locke.

The former is a vital component of all later theories of progress and ideologies based on them: liberalism, socialism, positivism, progressivism and almost all "liberation" ideologies. Hobbes and Locke are founders of the social contract and liberal traditions, which overlap somewhat but are not identical. What is perhaps most significant about these two is not so much the content as the method, eschewing (or downplaying) theological and religious arguments in favour of a mainly secular attempt to ground political thought.

The third component comes from the British Civil War and Commonwealth period (1640-1660). Not only the division between Roundheads and Cavaliers (the precursors of Tories and Whigs: see stage 3) but even the agenda of modern egalitarianism begins to emerge. This is exemplified not merely in the very rough equality of Hobbes but a more radical version due to the "Levellers" arguing that "every he and she" are equal to any other person.

### Stage 2

Modern Ideologies are the product of three distinct revolutions in the modern world. At the very least it can be argued that the basic ideological dichotomies of the present world



owe their origin to these distinct revolutions

It was the French Revolution that gave us the basic distinction between Left and Right. As indicated this will be attacked on logical and historical ground while acknowledging that a milder version (as argued by Tufte) has an influence on politics in democratic societies, a crucial qualification. Others have done the same for similar (but not identical) reasons: Samuel Brittan in *Left and Right: The Bogus Dilemma* and Hugh Graham in *The Vestibule of Hell*.

The Industrial Revolution produced indirectly the dichotomy between socialism and capitalism and the invention of the corresponding terms. Interestingly, the two terms were invented by one side of the debate, the Left side. What can be termed the Victorian Revolution gave us the terms “liberalism” and “conservatism”, terms that are the heirs of both “Whig” and “Tory” in 18<sup>th</sup> century Britain (and hence heirs of the British Civil War terminology).

### *Stage 3. Modern Ideologies*

We will begin with short definitions of the ideologies that emerged in the 19<sup>th</sup> and early 20<sup>th</sup> centuries. At the same time we must recognize that ideologies reveal internal dissensions. It is also an open question about whether they are *evaluative* rather than *prescriptive*. The safest claim is that they are both *diagnostic* and *prognostic*. They tell us what is wrong with society (or that it is basically healthy) and what to do to make it healthier, or to prevent the cure from being worse than the disease.

Most social scientists and philosophers are familiar with the fact/value or positive/normative distinction but the above distinction (prescriptive/evaluative) is not sufficiently noted. An example from ideological positions will illustrate this then definitions of various ideologies will follow.

The sentence “An Open Society is better

than any type of Closed Society” is an evaluative claim. It is not identical with, nor does it entail, a prescription such as “We should turn all closed societies into Open Societies”. So one could logically agree that the world would be better off if all countries were liberal democracies without feeling obligated to do so or without prescribing world-wide regime change towards that goal.

“Liberalism” is best defined etymologically since “Freedom” or “Liberty” is the key word especially free thought, free speech, freedom of religion, free trade and free association. It has morphed into a more egalitarian, statist creed in both the modern USA and elsewhere.

In its origins liberalism began as a reaction against two notable features of medieval society: religious conformity and ascribed status. While the Reformation undermined the former and the commercial and later industrial revolutions undermined the latter, the ideological war probably began with Hobbes (who is at least a proto-liberal) so far as liberalism is associated with secularization and modernity.

“Conservatism” is popularly seen as defensive of the status quo, of traditional values and as being both elitist and authoritarian. Today “conservatism” is taken in two different contradictory manners as an ideology (where it competes with other ideologies) or as a simple status quo philosophy where it is challenged. Thus people as different as Leonid Brezhnev and the Ayatollahs in Iran were/are “conservative” since they did/do not want radical challenges to their regimes. The contradictory interpretations are those that take it as similar to Fascism or as basically libertarian (or classically liberal) especially regarding the economy.

Gordon Graham argues that “conservatism” comes in three types: The first is really a version of classical liberalism

(= contemporary libertarianism). The second (which he associates with Roger Scruton) is too closely allied to Fascism or neo-Fascism whereas the third is what he labels “true” conservatism (typically British e.g. Halifax, Burke, Oakeshott, *The Salisbury Review*).

What Graham calls “True Conservatism”, may be the most appropriate use of the term even if few hold the view. He says of it “unlike political conservatism it has nothing in common with libertarian or classical liberal view” and it is not identical with Fascism either. Its’ basic creed is anti-Jacobin. This means it is opposed to any scheme to revolutionize or reform society in accord with some idealistic notion of the good whether this is defined by liberalism, socialism, fascism, Marxism, or free market capitalism. The anti-Jacobin feature is a useful reminder that modern conservatism begins as a reaction to the French Revolution. The opposition was manifold and variegated. For purposes of this article we can distinguish two types: the Burkean and the internal French enemies of the Revolution. Burke, famous for his *Reflections on the French Revolution* (1790) was actually a Whig not a Tory and favoured the American Revolution. He preferred the British system of slow gradual reform not rapid violent revolution. The main French enemies, De Bonald and De Maistre wanted to keep the Ancient Regime based on monarchy and the (Roman Catholic) church intact.

Socialism and Communism are related in an asymmetrical manner. This means “All Communists are Socialist” but “Some Socialists are not Communist.” It is what they have in common that concerns us here. These are basically two points. The first is that “Planning replaces the so-called Free Market” in the arena of production and that: second “Equality replaces inequality of wealth, income and power in the arena of distribution”. The planning is usually held to

be central planning. But there are decentralized versions of socialist planning as in anarcho-syndalism, workers control schemes such as market socialism and social democracy (discussed below).

There are two main differences between communism and socialism. The latter generally prefers peaceful, piecemeal reforms whereas Communism favours violent revolutionary overthrows of the system. The results aimed at differ in the following way: socialists want public ownership of the major means of production (factories, banks, mines, and so on) whereas communism envisions public ownership and bureaucratic control of almost all enterprises big and small.

Capitalism: It could be said that capitalist principles are a proper subset of Liberal principles, just as communism is a proper subset of socialism. Insofar as it is an ideology rather than a system then this is true since it means basically a free market economy, international free trade, free labor and minimal or no regulation except to prevent harm and fraud (as in J S Mill’s classical liberal principle that only harm to others can justify societal coercion or as in contemporary Libertarianism below).

The three main components of a capitalist system, private property, free competition or enterprise and the profit motive are often given separate rationales in ideological arguments. *Laissez-faire* may be the best known and most prominent capitalist ideology but it could hardly be said to be the most exemplified version of capitalism as either an actual system or as an ideology. Franklin Roosevelt and J.M. Keynes both claimed to be saving capitalism but certainly not the *laissez-faire* version.

Nationalism can be seen to be of two types, progressive and reactionary or left and right. It is also essential to distinguish it from patriotism. The latter, originally was an ideology of liberty. In the 19<sup>th</sup> century

nationalism was frequently allied with liberalism. The common thread uniting the two creeds is “the right to self-determination”. Liberalism applies this principle to the individual, the nationalist applies it to a collective entity: the nation.

Nationalism more often seems to ally itself with authoritarian creeds, both left and right. In the 20<sup>th</sup> century it has been preached (and practiced) by both the “extreme right” for aggressive imperialist purposes (Italy and Germany especially) as well as by the left as an anti-imperialist ideology in colonized and conquered nations (Asia, Africa and the Middle East). In each of these cases it can and has frequently allied itself with both secular (especially Marxist) and religious ideologies (Gandhi in India, Islam in Algeria and elsewhere).

### **Fascism and Nazism**

Both of these creeds are post-modern and while not reactionary they believe in radical inequality without the traditionalism of conservatism or the original Right, which emerged as opposition to the French Revolution. While Fascism and Nazism are often conflated, it is important to realize that only the latter was officially racist: i.e. believed both (1) Some races are intrinsically inferior and (2) have fewer rights than (or can be treated differently from) the “superior” race. Roger Eatwell defines Fascism as having two main components that distinguish it from non-Fascist ideologies: a holistic conception of the nation and an alternative Third Way economic alternative to both capitalism and socialism.

### **Anarchism and Libertarianism**

The main distinction between these two (non-identical) ideological twins is that the former advocate a society that is stateless and the latter a minimal state: one that only forbids acts that are harmful (or more precisely acts

that impose costs on others that are unwanted) but not all of them. Anarchism, it could be claimed (and has been by Gordon Graham), has no clear political implications. It might be thought that it would endorse libertarian social policy. However while it might seem obvious an anarchist would support decriminalization of drug use and restrictions on sexual behaviour or free speech, she might be reluctant to do so due to the fact that reform is often the enemy of revolution.

### **Populism and Progressivism**

The first of these can be defined with reference to the dictum “Vox populi vox dei”. It is the “democratic” equivalent to the divine right of kings (but without any theological implications: an agnostic or atheist could be populist). The second suffers from the familiar problem of defining what “progress” means. As indicated earlier in the origins of modern ideology this concept was crucial. It meant not only progress in knowledge but in human welfare as well.

But this leads to a crucial ambiguity: How is human welfare in a secular sense defined? How is it best realized? Is it by increasing freedom and/or equality? Or is it to be achieved by increasing some optimal combination of the two principles? While these two ideologies in their original guise are not as influential as they were a century ago their ideas live on in the post-1960 proliferation of ideologies, our next topic.

### **Stage 4. Post-1960 Ideologies.**

These late 20<sup>th</sup> century ideologies include “Liberation” philosophies for Blacks, women, gays, natives, animals and the environment. What is striking is that each of these creeds label themselves (or are labeled by others) as liberation ideologies but are closer to egalitarianism than they are to libertarianism.

What all of these ideologies have in

common is the promotion of greater equality especially for the groups mentioned: Blacks, women, homosexuals, animals and aboriginals. Here it may be useful to distinguish three different types or sources of inequality that are the targets of liberation ideologies. The three sources are race, class and gender. But what about human chauvinism itself, the idea that only humans have rights or ethical status and only human interests count when we make difficult moral or ideological decisions?

### **Ecologism**

While it can be argued that there are five different ideologies on environmental ethics, Vincent argues that there are two extremes, a “light anthropocentrist” wing and “Deep ecology” with a broad intermediate category further subdivided between “moral extensionism” and “reluctant holism”. The first “extreme” holds that, while only humans have rights, we should not show gratuitous cruelty to animals and the opposite extreme holds that all of existence should be given moral consideration. The intermediate categories hold that we should extend our moral concern from humans to sentient creatures capable of pain (animals) or perhaps to all life while holism holds that even ecosystems such as rain forests should be sacrosanct

### **Social Democracy and Neo-Conservatism**

It may seem strange both to lump these two together and place them under post-1960 ideologies since both clearly precede the 1960s. Both are compromises with earlier predecessors. Social Democrats, especially in Europe have considerably weakened their hostility to the market, most liberals have abandoned *laissez-faire* and it is an open question whether Neo-conservatism is even a proper subset of conservatism. Walter Russell Mead has the following interesting comment:

Some American conservatives regard the Bush administration foreign policy as “Neo-Jacobin” not a compliment in the conservative vocabulary.

The godfather of this movement is allegedly Leo Strauss, a German Jewish emigrant from Nazi Germany. The (alleged) fact that the movement is primarily due to American Jewish thinkers (with *Commentary* as its main journal) then explains its striking difference from traditional conservative and Right wing policies with their anti-semitism and/or white racism (the Old South) and anti-democratic, elitist tendencies.

Why then the rubric neo-conservative? Neo-conservatives, while generally “pro-market”, are less so than libertarians mainly due to their pro-family policies and are in general less hostile to state intervention wanting to reform the welfare state not abolish it. So their real godfather may be Freidrich von Hayek, who rejected the term “Conservative” for himself but plausibly fits the neo-conservative label better than Leo Strauss.

Social democracy has kept a weaker version of the egalitarian redistributionism of 19<sup>th</sup> century socialism (usually called “social justice”) while surrendering the more radical idea of public ownership, planning and control for the milder idea of regulation and intervention. It is an attempt to reduce inequality or abolish poverty rather than eliminate inequality or reduce to a very low level.

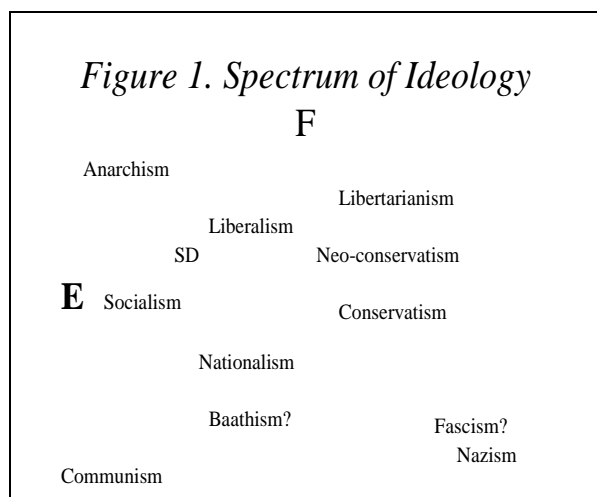
### **Who’s Left? What’s Right?**

My basic objection to this time-honored system of nomenclature is a combination of historical and logical. The only reasons I can see for its continued use is (a) convenience (b) an ideological motivation on both sides.

The stages of the argument are: First historical. We have seen briefly how the three dichotomies above evolved, but not how they

were subsequently conflated and confused. That is another long, convoluted story (see Part V on Hugh Graham's explanation). Since we can't thoroughly explore it we will instead jump to the second, more crucial logical argument. This rests on two key premises: first, that is it absurd to lump together the following three groups: defenders of the 18<sup>th</sup> century French Ancient regime (= Old Regime Right), post-modern fascists and free market defenders. The one and only principle they can plausibly be said to have in common is anti-egalitarianism. Second, it similarly unites anarchists, Leninists and Social Democrats on the same side with only the opposite principle, egalitarianism, in common.

The main problem with this is that it gives us a one-dimensional political man forced to choose between ideologies solely on the basis of equality versus inequality. The advantage of the Cartesian grid substitute that I propose (for which however no originality is claimed) is that it introduces the dimension of liberty. On the traditional spectrum both communism and anarchism are on the left side whereas fascism and libertarianism are on the right side, a transparent logical absurdity.



□ □

In the above F= Freedom and E = Equality so we have a vertical and horizontal aspect. SD = Social Democracy. (I have put question marks beside a couple of difficult-to-classify

ideologies.) The conflict between liberty and equality creates a huge internal problem within modernity itself. Should “progress” be defined with reference to increased liberty or increased equality? Or both? Or neither?

Finally, it seem clear that there is a difference between the Old Regime Right and 20<sup>th</sup> century creeds classified as “right wing”. The Old Regime Right did want to turn back the clock and was “reactionary”, cleaving to “throne and altar”. Fascism, as Mussolini emphasized, was not reactionary but revolutionary. This is why it can reasonably claim to be the first post-modern ideology not a pre-modern nostalgic desire to return to the good old days. Unlike the Marxism he once espoused, Mussolini saw an anti-egalitarian future. The same is true of libertarianism: whereas the Old Regime Right preached “Throne and Altar” the 20<sup>th</sup> century “extreme” right preached “Nation and Race” and the so-called New Right (or neo-conservatism) preaches “Market and Family”. However, a libertarian, unlike the Old Regime Right or the extreme right will not force inequality on people but will permit it under free market conditions. Neither libertarians nor neo-conservatives resemble the old Right except for opposing radical egalitarianism.

A different system of classification would be based on the difference between Open and Closed societies. This would put authoritarianism and totalitarianism on the same side with democrats and cosmopolitans on the other side. This approach harmonizes well with Ball and Dagger's distinction between democracy as an ideal and ideologies which can then be defined by their attitudes towards democracy.

The term “totalitarianism” was invented by Mussolini in 1925. The term “Open Society” was invented by Bergson in 1932. The former was subsequently developed both by political scientists and defenders of

democracy in ways incorporating both descriptive and evaluative connotations. It is doubly ironic then that it was Mussolini's invention since he clearly did not mean it in a pejorative sense.

The basic idea, as it evolved, is "Total control of society's major institutions". It does not mean total control of every aspect or facet of society much less controlling everyone's life but it does mean control of independent organizations or institutions such as the economy, education, organized labor, religion, the press and culture. Ideology is also seen as intrinsic to totalitarianism. The term itself does not designate an ideology but a political system motivated by ideology to exert total control.

Similarly authoritarianism is a system of government, often without any official ideology, aiming at less than total control but with sweeping restrictions on individual liberty. These can be imposed in the interests of modernizing a traditional society or simply to preserve the status quo (or at least the power and privileges of its rulers).

Two interesting questions arise: was Marxism always a totalitarian ideology or was it a political philosophy misused to justify the most purely totalitarian society of the last century? The main reasons on both sides of this debate are: first that Marx saw the "dictatorship of the proletariat" as a temporary but necessary step to the eventual withering away of the state so the free development of all would result from a classless and (therefore) stateless society. However if one looks closely at the ten point program in the Communist Manifesto, then one can easily discern the seeds of Stalin's policies of the 1930s especially points 1, 2, 5, 6 and 7 regarding collectivization and nationalization of land, banks, commerce and industry.

Curiously the major Fascist leaders, Mussolini, Hitler and Oswald Mosely all saw

themselves as borrowing from both left and right. The original Nazi 25 point program did contain genuine elements from both nationalism and socialism. This leads logically to the question: "Does Ideology make a difference, logically or pragmatically?"

### **Ideology And Public Policy**

Edward Tufte argues effectively that ideology does effects political decisions both on the side of politicians and voters. In his key chapter the main point concerns tradeoffs between party positions on inflation and unemployment. This applies primarily to the USA but he also includes data on Sweden, Great Britain and the Inflation Unemployment Relation in 12 countries as well as on debates and issues regarding income redistribution. This is a very mild Left/Right distinction, if it is that at all. He then argues in the next chapter that politicians' accept the theory that their ideologies make a difference (to the electorate) and that this theory is confirmed by the electorate's behaviour.

While I agree with G. Graham's desideratum that ideologies should make a difference, I will point out some problems with drawing logical implications from particular ideologies. Let us take the most prominent thread of what is now called political correctness: "the egalitarian principle", which will be defined as follows: "We should reduce inequality in society as much as possible, especially that which lacks any clear or plausible rationale". What, if anything does it imply for issues such as animal rights, abortion, capital punishment, homosexual rights and the welfare state? Here some ambiguities in "egalitarianism" come out.

Peter Singer is the inventor of the term "speciesism", a word deliberately chosen on the analogy of "racism" and "sexism". Singer

wrote an article called “All animal are equal”. But he seems to use this in an Orwellian manner without realizing it. For him some animals are still more equal than other i.e. humans. We have duties as well as rights, whereas all other animals have rights but no duties. This is a rather significant point that many discussions of rights today seem to miss including discussion of welfare rights. Unlike Marx and Engels in the Communist Manifesto, modern animal rights and welfare rights proponents do not include a principle of equal duties as well as equal rights.

Abortion seems easy to defend on both egalitarian and libertarian grounds. Surely if women are to be both free and equal to males they must have the right to choose whether or not to be mothers. But does the fetus then not count in either the utilitarian or rights calculus? Furthermore what happens if many parents decide to abort if the future child is to be female rather than male or if it will be healthy rather than unhealthy and/or disabled? And how unhealthy and disabled? Does this not open the door to eugenics, a policy generally despised by egalitarianism but not utilitarianism which has a general egalitarian starting point?

Bentham’s utility principle treated all pain and pleasure as equal (if judged so by the recipient) and he included animals in his “felcific calculus”. Kant’s “respect for persons” however only extended to humans.

What many people, who may be skeptical about the sincerity of Far Right ideologies like Fascism and Nazism to combine both left and right components may not realize, is how much Stalinism did this. While Stalin was engineering the greatest economic revolution in history, he was also introducing a very conservative “counter-revolution” in the areas of family and sexuality. Whereas the Bolsheviks of the 1920s were “permissive” in policy areas such as extra-marital sex, marriage, abortion, equal rights for women

and educational experiments, the 1930s saw a set of policies that could be seen as outright reactionary. Homosexuality was made illegal in 1934. Every communist society has followed suit and only East Germany ever altered this policy. To this day it is illegal in Castro’s Cuba. In fact pre-marital sex was prohibited in all communist societies.

Egalitarianism also turns out to have several definitions. Both Kant’s respect for persons and utilitarianism are egalitarian but in very different ways just as liberalism and socialism are egalitarian but in strikingly different ways. Perhaps the key tension in modern progressive ideologies is the tradeoff between the two.

Consider contentious issues heatedly debated the past few decades: pornography, affirmative action, pay equity, free speech and positive rights. These all involve conflicts between libertarian and egalitarian principles. A feminist may oppose pornography and advocate restriction on grounds of promoting equality whereas a libertarian will object to censorship. Positive rights, unlike negative rights, require action to benefit others rather than merely refraining from inflicting harm. They are also usually seen as requiring government interference including increased taxes, which are seldom paid voluntarily.

### **End of History and Non-Rationality**

In the 1950s Daniel Bell wrote a controversial book entitled “The End of Ideology”. In 1989 with (European) Communism on the verge of collapse Francis Fukuyama wrote an equally contentious article called “The End of History”, later turned into a book. In between the two events occurred the outburst of new ideologies in the 1960s usually associated with the New Left. Then the 1970s saw significant creative work in political philosophy: John Rawls, Robert Nozick, and Alan Gewirth.

What Bell and Fukuyama seem to have in

common is the following claim: we have reached the end of significant ideological debate. This can be summarized in Fukuyama's own words: "There exists no systematic, viable alternative to liberal individualism." This is a claim that seems to be both empirical and normative at the same time. Fukuyama's definition of liberal individualism consists of two principles and two (or three?) institutions. The former are liberty and equality. The latter are democracy and a (relatively) free market tempered by a moderately redistributive welfare state.

This opens up the possibility of rational debate in two different ways. First: anarchism, utopian socialism, Marxism and fascism can be seen as systematic but as either never viable or no longer so. Islamic Fundamentalism as a political creed may well turn out to be viable but not systematic as an ideology rather than as a religion.

On the other hand if someone produced a systematic viable alternative then the theory will be refuted. Some such as Alasdair McIntyre concede the point that at the moment there is no tolerable alternative to liberal individualism but he concedes this without enthusiasm and seems to hope someone will carry out such a task.

The final reason for arguing that ideologies can be rationally evaluated is that they include explanatory and descriptive as well as prescriptive or evaluative components. Explanatory theories are supposed to be subject to rational evaluation if any theories are. The argument that ideologies are intrinsically not rational due to the evaluative and/or prescriptive component usually rests on logical positivist dogmas about empirical verifiability and logical proof. However, positivism is one of the most thoroughly refuted theories in 20<sup>th</sup> century philosophy of science.

While a long detour into this contentious topic is not possible nor desirable the

following short summary (due to Bruce Caldwell's brilliant *Beyond Positivism*) will suffice: The original logical positivist program of verificationism quickly gave way to two alternatives, logical empiricism (watering down verification to confirmation) and Popper's falsificationism. Both of these however have run into formidable if not insuperable problems and have been replaced or altered by "growth of knowledge" theories, (Thomas Kuhn, Imre Lakatos, Paul Feyerabend and Popper also). Hilary Putnam recently claimed that the fact/value distinction has collapsed.

The argument here does not need to go that far. All it needs is something such as the following: the alleged radical epistemological difference between positive and normative in its original Weber/Robbins view is no longer defensible. Since ideologies include components also found in political science theories, they are allegedly refutable or confirmable or face problems not greater than scientific theories do.

Further it is arguable that normative theories such as claims about human rights can be subject to the same types of rational debate found elsewhere: as the author has argued elsewhere (Hayes, 2001) normative claims have existential, factual and logical and theoretical implications that make them as criticizable or refutable or confirmable as other theories. Any claim that humans have right entails logically that other have duties and since "ought implies can" these claims imply is-statements which are, in principle anyway, refutable or verifiable (even if philosophers of science cannot give a precise account of how). The problems here concern the positive or factual side of the dichotomy. They are not due to the almost sacrosanct Weber/Robbins dichotomy.

### **The Explanation of Ideology**

There are two interesting general



explanations of ideology due to Emmanuel Todd and Hugh Graham. The former is more specific to Europe although he claims it applies beyond its confines since he applies it to communist regimes in Asia as well as the former USSR. His model is institutional whereas Graham's is more intellectual. The latter is also somewhat broader since it embraces the Eurasian super-continent.

Todd draws an interesting parallel between four types of family systems based on the equality-liberty dualism used in the substitute political spectrum just constructed. According to Todd, the British family system is simultaneously libertarian and non-egalitarian. The French family system is both libertarian and egalitarian, the German is neither and the Russian is egalitarian and authoritarian (hence non-libertarian). This corresponds (he says not unreasonably) to the major ideologies we associate with them: classical British liberalism (and laissez-faire capitalism) the French Revolutionary trio *liberte, egalite plus fraternity* which is an extension of equality. Nazi Ideology was anti-liberal and anti-egalitarian whereas Communism was officially egalitarian but also extremely authoritarian if not totalitarian. If Alan McFarland is correct the roots of English individualism go far back into medieval England. The first two German Reichs before Hitler's Reich seem to exhibit the same characteristics (the Holy Roman Empire and Bismark's Reich) but it might be a stretch to apply the same to pre-Revolutionary France and Tsarist Russia.

Graham's theses are extremely complex and difficult to summarize but he sees a continuity in Western thought which is thoroughly rooted in ancient Eurasian (especially Aryan thought) as well as that of ancient Israel. The key components in his argument are that the monism of Greek philosophy logically entailed dualism which opened the door to Gnostic religion and

philosophy with its radical dualism.

Modern ideologies then are basically a secularization of Gnostic religious ideas: the fall of man into a world of evil accompanied by the possibility of redemption or salvation via *gnosis*, one of the Greek words for "knowledge". The origins of Utopian thought are found here when suitably secularized. Political theories of such salvation are just as divided concerning the one true way of salvation as religious views have been and this led by a complicated route to the modern left-right distinction. He regards it as obsolete for much more complicated reasons than those presented here. His schema may be a Procrustean bed but he makes some interesting points along the way, as does Todd.

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## Income Inequality and the Distribution of Power

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### **Introduction**

Income inequality can very simply be defined in terms of a gap between the haves and the have-nots. When applied to a country's income distribution it means that those at the top of the distribution hold a greater share than those in the middle and those at the bottom. Over the last couple of decades there has been a considerable increase in income inequality in much of the western industrialized world. Generally speaking, income inequality in the United States has been greater than other industrialized countries as measured by Gini coefficients, the ratio of the top quintile of family income to the bottom quintile, and the share of wealth held by those at the top relative to that held by those at the bottom, as evidenced by Table 1. And yet, inequality in underdeveloped and developing countries lacking in sophisticated welfare state programs and where economic reforms, including land reforms, have not occurred, tends to be much higher than in the industrialized ones, including the United States.

Inequality, however, may be greater in countries that are in the process of transitioning to market economies. China serves as a good example where inequality was relatively low during the first years of Communist rule, especially when land reform was introduced. But it rose precipitously during what has been referred to as the Great Leap Forward and Great Famine from 1957-196, reaching an all-time high in 1966. Though it declined afterwards, it began to rise again in 1987 after the government began undertaking market reforms (Kambur and Zhang 2001; Benjamin et al 2008). Wang Xiaolu (2006) notes that the Gini coefficient

was 32.0 in 1980, dropped to 25.7 during the initial stage of economic reform between 1980-1984, but increased to 35.5 in 1990 and then 44.7 in 2001.

Although free markets may be viewed as the source of inequality, the question remains: why is it greater in some countries than others? The simple answer is that the politics of a nation and the public policies that it pursues has much to do with the level of inequality. Short of adopting socialist policies, there is no way to really end it. But inequality can be lessened when a country seeks to pursue policies that bolster the least advantaged members of society.

This essay will explore trends in inequality and the various measures of it, and will also look at its impact on the distribution of power. While income inequality is a problem inherent to all capitalist economies, it tends to be greater in those countries with less of a social safety net. Indeed, it has risen in those countries where as a matter of deliberate public policy the social wage has decreased.

Income inequality, however, is more than a matter of distribution; rather it has serious repercussions for democratic theory because to the extent that it results in some having more resources than others it seriously affects the distribution of political power and ultimately the outcomes of a democratic political process. The privileged participate more than others and tend to be better organized to press their demands on government (Jacobs and Skocpol 2005). The reality, however, is that one cannot have true democracy amidst rising income inequality because in the end not all in the political process are equal.

### **Measuring Income Inequality**

Measuring income inequality is really no easy task. Four widely used measures of income inequality are the Gini coefficient, the Atkinson inequality index, the Theil

inequality index, and the coefficient of variation.

The gini coefficient is a summary statistic ranging from 0 when all individuals are equal to 1 where there is complete inequality, and it tends to be very sensitive to changes around the median. Developed by the Italian statistician Corrado Gini in 1912, the index represents a percentage which is equal to the Gini coefficient multiplied by 100. A coefficient of .70, for example, would suggest extreme inequality, whereas a coefficient of .13 would suggest relatively low levels of inequality. How countries compare using this index can be seen in Table 1. Whereas most developed European nations have Gini coefficients between .24 and .36, the United States tends to have a coefficient above .4. And many Central and South American countries, as well as African countries, have Gini coefficients close to .60 and in some cases exceed it. The Gini coefficient, however, may not be the best measure when comparing large countries to small countries. Moreover, because benefit systems vary from country to country, comparisons of inequality between countries may also be difficult using this measure.

The Atkinson index explicitly incorporates normative judgments about social welfare and is derived from calculating an equity-sensitive average income based on a per capita income that would result in the total welfare being exactly equal to the total welfare generated by the actual income distribution if everybody enjoyed the same per capita income. The Atkinson index is sensitive to inequality changes in the lowest part of the income distribution. Therefore, as equity sensitive income rises, more social weight is attached to income transfers at the lower end of the distribution. The Atkinson index in economics is specifically used to quantify income inequality. And more

specifically, it is used to gauge movements in different segments of the income distribution.

The Theil inequality index, derived from the econometrician Henri Theil, ranges from 0 to infinity with higher values representing greater equality. It is essentially a mathematical formula:

$$(1) \quad T = \frac{1}{N} \sum_{i=1}^N X_i \left( \frac{x_i}{x} \cdot \ln \frac{x_i}{x} \right)$$

In the formula,  $x_i$  is the income of the  $i$ th person,  $x$  is the mean income, and  $N$  is the number of people. The first term inside the sum represents the individual's share of aggregate income, with the second term representing that person's income relative to the mean. When everybody has the same mean, the index is equal to zero, but when one person has all the income, the index is equal to  $\ln N$ . An advantage to the Theil index over say the Gini coefficient is that it is the weighted sum of inequality within subgroups. As an example, inequality in the U.S. would be the sum of each state's inequality weighted by the state's income relative to the entire country.

And the coefficient of variation is simply a statistical measure of the deviation from the mean. It measures dispersion of a probability distribution, defined as the ratio of the standard deviation  $\sigma$  to the mean  $\mu$ . As a number without dimensions, the coefficient of variation allows for a comparison of populations that have significantly different mean values. This measure is often used to discuss the normal distribution for positive mean values that have a standard deviation significantly less than the mean. The coefficient of variation, as is also the case with the Theil index, tends to be very sensitive to changes at the top part of the income distribution.

Depending on which measure is used, the degree to which there is inequality will vary.

All of these measures belong to groups of relative inequality measures that are not necessarily sensitive to relative changes in income scale, but do imply some *a priori* value judgment about the distribution itself. On the basis of data from the Luxembourg Income Study (LIS) Brigitte Buhmann, Lee Rainwater, Guenther Schmaus, and Timothy Smeeding (1988)) found that when using the Atkinson index, the United States had the highest inequality in disposable income, followed by the Netherlands and Australia. Sweden and Norway, by contrast, had the most equally distributed income. And yet, on the basis of both the Gini coefficient and the coefficient of variation, the Netherlands actually had more equality relative to other countries.

To these four measures may be added yet another: the ratio of say the mean or median income of those at the top of the distribution to the mean or median of those at the bottom of the income distribution. This can be done through a quintile analysis or perhaps even a decentile one. The problem with measuring inequality, regardless of which approach is taken, is data. Researchers often rely on official income figures from say a national census. In the United States, for instance, this can be quite problematic because the U.S. Census bureau top-codes the income variable usually at \$1 million, whether it be personal, household or family. This means that in a city like New York City, for instance, where there may be a disproportionate number of those earning more than \$1 million, the extent to which there is income inequality is understated (Levin-Waldman 2001).

Various researchers have tried to get around this problem by using 10-50-90 percentile levels to analyze the distribution rather than quintile distribution. This avoids the top-coding problem largely because it excludes those over the 90 percentile level. And yet, most of the skew comes from that

top 1 percent that has now been eliminated. Even though these techniques will avoid understatement of income inequality, the fact remains that a comparison of the 10-90 percentiles of the income distribution still eliminates the top 10 percent where a disproportionate share of family income happens to be. As Table 1 makes clear, those countries with high Gini coefficients also have significant proportions of wealth and/or income held by the top 10 percent. An example of inequality using this approach for OECD countries during the mid 1980s can be seen in Table 2. Again on the basis of the ratio of the 90 percentile to the 10 percentile, the United States has the highest rate of inequality at 5.94 compared to Finland with the lowest rate of 2.59.

### **Rising Income Inequality**

To talk about income inequality is somewhat problematic because it isn't entirely clear just what we mean by it. What does it mean to say things are unequal in terms of distribution? Income inequality is often viewed as a problem in a market economy, which allocates income on the basis of several factors including education, experience, innate abilities, incentive, and risk. On the contrary, when these factors are considered income is by and large distributed on the basis of desert. More educated individuals, and those possessing greater abilities, are entitled to earn higher incomes than those who do not. That one is poor, especially in a society where everyone is presumed to enjoy equal opportunity, is ultimately that individual's responsibility. And yet, the capacity to have greater income exists if there is a willingness to obtain the requisite education and training to command it. Although there may be some agreement that a more equitable distribution of income ought to involve a move to greater equality of income and greater equality of opportunity,

the prevailing view, at least in the United States is that there is equality of opportunity (Robinson & Dervis 1977).

According to Leslie McCall (2001), the problem is that we tend to look at the income distribution in more absolute terms whereby we compare those at the top of the distribution to the bottom. In reality, there is what she calls “configurations of inequality” in which race, gender, and class intersect in a variety of ways depending on underlying economic conditions in local economies. There is in fact no local economy in which all types of wage inequalities are systematically and simultaneously lower or higher; rather the norm is a complex intersection of various dimensions (p 6). Therefore, inequality needs to be conceptualized as the outcome of both economic restructuring and gender and racial divisions of labor. Inequality will also vary among age cohorts.

Income inequality and poverty are both greater in the U.S. than elsewhere. On the basis of the LIS, Smeeding and Dennis Sullivan (1998) explored differences in economic well-being across cohorts of the population in four modern nations: Canada, United Kingdom, Sweden, and the United States. Using adjusted disposable income (ADPI) as the household’s principal measure of well-being, both the U.S. and U.K. were found to have experienced between 1974-94 rapid secular increases in inequality and in relative poverty. Inequality increased less in Canada and Sweden, where poverty levels were also lower. As they observe, overall levels of inequality differ markedly across these nations, and the differences are reflected in their poverty rates.

While the U.S. has had the highest relative poverty rates, Sweden has had the lowest. Younger households (under age 30) in the U.S. are not doing as well as older ones (over 65), but both the young and the old have higher poverty rates than other nations. Those

with the highest incomes and the lowest poverty rates in every nation are middle-aged (40-54) families. John Coder, Lee Rainwater and Timothy Smeeding (1989) found that in a comparison of ten modern nations, the most equally disposable income was in Sweden and Norway, and that the highest degree of inequality was in the U.S., Australia, and Canada. Newer countries like the U.S., Australia and Canada tend to have more poverty and fewer people in the middle class than do older nations, and the Scandinavian countries tend to have the least poverty and the largest middle class. But among the elderly, the U.S. while it ranks behind the U.K. and Israel, has the highest poverty rate. It also had a higher fraction of children living in poverty.

Despite a consistent increase in inequality in the U.S. since 1979, the rate of increase has not been constant. The sharpest increase occurred during the early 1980s and was followed by a flattening during the later 1980s. Then during the 1990s income inequality began to re-accelerate (Bernstein and Mishel 1997). The average weekly wages of men, for instance, increased by about 20 percent between 1963 and 1989, but these gains were not spread equally. Wages for the least skilled, as measured by the 10<sup>th</sup> percentile of the wage distribution, fell by about 5 percent while the wages of the most skilled, as measured by the 90<sup>th</sup> percentile, increased by about 40 percent (Juhn, Murphy and Pierce 1993). The net result of this divergence was an enormous increase in wage inequality. At the same time, many of the jobs that were created were at the low end of the wage scale. The majority of these low-wage workers in the U.S. have no educational credentials beyond a high-school diploma, and many, including a large number of immigrants, lack even this credential. Eileen Appelbaum, Annette Bernhardt and Richard Murnane (2003) refer to these workers as

frontline workers. At the same time, a college education and low-wage work are not necessarily mutually exclusive.

### **Sources of Inequality**

The theory of perfectly competitive markets blames rising inequality on structural changes in the economy that have resulted from a mismatch between good paying jobs and the skills available to workers. The main culprit is technological change biased towards those with higher levels of education and skills (Juhn, Murphy and Pierce 1993). According to this school of thought, the labor market is divided into a primary market where high premiums are placed on skilled workers, and a secondary market where unskilled workers are trapped in the lowest-wage service sector of the economy. The growth in wage inequality between the primary and secondary labor markets has been caused by increasing skills differentials between the two (Katz and Murphy 1992; Katz and Krueger 1992).

Increasingly, greater attention in the literature is paid to institutional factors like wage-setting institutions and social norms. Institutionalists hold rising wage inequality to be due to a shift in public policy and a corresponding decline in labor market institutions like unions and the minimum wage in the U.S. and wage councils in Britain (Piore 1995, Gordon 1996, DiNardo and Lemieux 1997, Fortin & Lemieux 1997, Lee 1997, Machin 1997, Galbraith 1998, Palley 1998, Lemieux 1998, Howell 1999, Wallerstein 1999, Craypo and Cormier 2000). During the late 1970s, the United States began experiencing a sharp ideological shift towards a preference for competitive market outcomes and solutions, and this ideological shift did have direct effects on bargaining in the workplace (Moody 1988).

Examining trends in overall wage inequality in the United States labor market on the basis of data from the Current

Population Survey (CPS), David Card and John DiNardo (2002) attributed overall wage inequality in the U.S. at least during the early 1980s to trends in the minimum wage and declining unionization. And in data on worker literacy in OECD countries, David Howell and Friedrich Huebler (2001) found that while there was a positive association between skills differentials and changes in wage inequality, there was also a strong association between labor market institutions and changes in wage inequality. This would suggest a global role for institutions to affect inequality.

Peter Gottschalk (1997) suggests that income inequality increases when the growth of income is greater among those at the top than among those at the bottom, even though bottom incomes have improved in absolute terms. While mean wages grew rapidly during the 1950s and 1960s in the U.S., the dispersion around the growing mean changed very little. But as mean wages grew slowly during the 1970s through the 1990s inequality rapidly increased. So long as those at the bottom of the income distribution gained along with everyone else from secular growth in the mean, it was a foregone conclusion that poverty rates would be kept down. Moreover, countries with the greatest increases in income inequality were also those that had the most decentralized labor markets. On the contrary, those countries with centralized wage-setting institutions tended to have less income inequality. And as data from the LIS demonstrates, those countries with greater welfare provision and other welfare state institutions that serve to boost the incomes of those at the bottom tend to have lower levels of income inequality (Kenworthy 1999).

### **Social Effects of Inequality**

The most visible effect of income inequality is perhaps poverty, but because poverty isn't something that affects most people we may

not easily see the connection between inequality and poverty. And yet, as Mark Rank (2004) argues, poverty, just like income inequality, results from failings in economic and social structures. Much of the current research does establish that individual and family characteristics do have an effect on whether one is likely to experience poverty during one's lifetime. There are particular attributes and characteristics that place individuals at a disadvantage in the labor market.

Kathryn Neckerman (2004) argues that economic inequality by itself would of course be a cause for concern, but its impact is only compounded by its social consequences. There has been a rise in social inequality in many different realms such as family life, education, or civic engagement. Social inequality in these realms only magnifies the burden of rising poverty for the most vulnerable, and thus sustains for a long time the effects of inequality. Neighborhoods with high concentrations of poverty and scarce social resources have been linked to developmental problems for children living in them. Educational inequality has its most immediate consequences in the labor market with new workers being sorted into good jobs and bad jobs. Then there are perhaps effects of economic inequality on the political system.

Between the 1970s and the 1990s, in the U.S. for example, at a time when social and economic inequality was increasing, there was also a divergence of family patterns across social and economic strata. A well known changing family pattern was a shift in family structure. There was a dramatic increase in single-parent families, and it is this particular shift in family structure that has been identified as a factor exacerbating income inequality. Single parenthood appears to be most common among socially disadvantaged groups, and single parenthood

also appears to compound social disadvantage in numerous ways (Martin 2004).

According to David Ellwood and Christopher Jenks (2004) not only has family structure changed from 1900 through the late 1960s, but it has changed very differently depending on parents' education and race. From an economic perspective, the most bewildering feature of family change has been the spread of single-motherhood, which in turn has played a major role in the persistence of poverty. Single-parent families have less income than two-parent families. Although children living with stepparents in adolescence have about the same family income as those living with their biological parents, they are also more likely to drop out of high school or to have a child while still a teenager. In this vein, children living with a stepparent are at least as disadvantaged as children living with a single parent. Mothers' educational attainment rose substantially between 1960-2000, but during the first score of that period the percentage of mothers who were unmarried also rose sharply throughout the educational distribution.

Traditional economic models treat marriage as a contract from which both husbands and wives expect to reap economic benefits. Structural changes in the economy no doubt affect those expectations. One of the popular explanations for the rise of single-motherhood is that women are less willing to "put up with" the way men treat them (p.52). But in virtually all models and samples, weaker economic performance is associated with reduced or delayed marriage, and they do find some evidence that improving job opportunities for men has somewhat increased marriage and reduced single-parenthood. Theoretical and empirical literature for women, however, has been far more ambiguous about the effects of female labor market opportunities. But improved



opportunities for women may have led them to postpone childbearing.

Steven Martin (2004) suggests that delayed family formation may actually be most common among socially advantaged groups, and it may thus confer comparative advantage in numerous ways. Those who delay family formation tend to be better educated and when they do decide to form families, they are in better financial positions to pay for high quality child care and thus greatly reduce their lost career time, which also carries with it a deficit in income. Economically successful women in particular tend to have a smaller wage penalty associated with having children. Although increases in income inequality have not been the sole, or even the primary, cause of declining early adult marriage and marital childbearing, it does nonetheless appear to be an important factor in how families adapt to new opportunities and constraints.

Rising income inequality may have been affecting social inequality by increasing residential segregation along income lines as well as ethnicity. Recent research on the neighborhood effects of income inequality suggest that neighborhood characteristics such as poverty, crime, and residential turnover influence several interrelated aspects of the neighborhood environment, which in turn affect families and children. Advanced industrial countries have gone through a process of economic restructuring assumed to be strongly associated with the process of globalization. As a consequence of these larger economic trends which have exacerbated income inequality, there has been social polarization, which also varies from country to country (Musterd and Ostendorf 1998; Hammett 1998). Similarly, Andrew Beer and Clive Forster (2002) note that during the 1980s and 1990s, the Australian government embraced international processes of economic change designed to transform the

economy and hasten the emergence of the new economic order. As a consequence, income inequality between 1976-1981 increased as income of the poor fell, but after 1981 it increased as the wealthy became wealthier.

These trends have a particular effect on European cities, where spatial segregation tends to be more visible. European cities have generally been experiencing a growing problem of social exclusion, aggravated by spatial segregation, especially concentrated among disadvantaged groups. These disadvantaged include the unemployed, the young and the unskilled. As much as there may be any number of explanations for social exclusion, a common underlying factor is change in economic structure, stemming from global competition and technological innovation. Changes in economic structure have resulted in both simultaneously an under-representation of unskilled workers—the most rapidly declining group—and an increase in jobs requiring greater skills (Slouten 2000). And yet, in Western societies polarization tends to be mediated by the structure of welfare provision and taxation.

Sako Musterd and Wim Ostendorf (1998) note that in Amsterdam, social exclusion related to the lack of social participation is especially a problem. Social exclusion, then, is one of the most important potential consequences of many of those processes related to social problems. In Sweden disadvantaged people tend to cluster voluntarily or involuntarily, in isolation from mainstream social and economic activities. Addressing income inequality has long been an overarching political goal. The government has also attempted to mix different groups of households in ‘integrated housing’ — ideally a mix of households with different demographics, socio-economic and ethnic characteristics. Swedish welfare policy has also been focused on economic resources.

An ideological cornerstone of the Swedish welfare state has been equality between households, despite demographic, socio-economic and ethnic characteristics, as well as residential patterns (Borgegard, Andersson and Hjort 1998).

Mechanisms of segregation fall into four categories: child and family related institutions; social organization and interaction; normative environment; and labor and marriage markets. Child and family-related institutions include schools, child care providers, public libraries, recreational programs and activities, parks, religious institutions, and social service providers. Economic models, of course, suggest that labor and marriage markets are key elements in the neighborhood effects on families and children. The normative environment includes neighborhood norms that may be a consequence of characteristics of people who live in the neighborhood such as their income level, ethnic background, education, or immigrant experience.

Norms may also be affected by social organization and interaction and also by marriage and labor markets. The central idea in the normative environmental literature is “that the greater the concentration of like-minded people, the stronger the normative climate and the greater the exposure of neighborhood residents to these norms” (Pebley & Sastry 2004:122). The central question may well be whether children who grow up in poor neighborhoods are worse off than other children. And are disparities in children’s welfare by neighborhood poverty level due to differences in their family characteristics, or do neighborhood conditions themselves play a role?

Robert Haveman et al (2004) maintain that as family income inequality increases, those families below the median are further from the social norm than before. Similarly, those at the top of the distribution see a larger gap

between themselves and the rest of the population. Many fear that the growth in income disparities among families has had a variety of adverse consequences for both families and communities. The question is how changes in overall income inequality may affect children’s attainment. What is clear is that the growing economic distance between people can reduce common interests and increase social separation.

Families at the bottom of the distribution may end up drifting further from the mainstream, and thus may also experience greater alienation as those with greater resources may come to see them as both more distinct and undeserving. This may also have consequences for how citizens in turn view the potential role and functions of government. Haveman et. al. argue that when studying the potential effects of growing family income inequality, it is particularly important to consider trends in the level and inequality of inputs in children’s attainments, and also the trends in those attainments. Looking at three key indicators of family inputs—parental education, family structure, and family size—they conclude that the situation for children has improved substantially on both parental education and family size but worsened on family structure.

The standard assessment of labor market performance uses employment and earnings over time, but these indicators combine both opportunities in the labor market that are open to people and their choices regarding labor supply and work. While they found evidence that both the level of family resources and the level of attainment of young people have improved over time, they also found limited evidence that better quality of what might be thought of as social capital, i.e neighborhood quality and school quality, is associated with better outcomes.

Insofar as schools are financed through property taxes, residential patterns along

income lines will also result in unequal schools. Schools with well-stocked libraries, for instance, may because of their symbolism attract higher quality teachers and educationally involved parents who can convey the importance of reading to children. Moreover, inequality increases at the margins every time a high-achieving student, a very involved parent, or highly qualified teacher moves from a poor or predominately minority school district into a whiter or richer one (Phillips & Chin 2004).

Inequality in social capital will consequently further exacerbate inequality to the extent that it affects access. As a consequence of inequality different groups will be socialized differently. Pierre Bourdieu couches the relationship in terms of what he refers to as *habitus*, a pattern of beliefs and behavior based on the experiences of living among certain classes or groups. As Pekka Sulkunen (1982) explains, “the habitus of a group or a class defines a symbolic order within which it conducts its practices—in everyday life as well as in the feast. It provides a common framework within which the members of the group understand their own and each other’s action” (p.108). Based on *habitus*, the styles of working class individuals, particularly in France, are functional, which is the polar opposite from intellectuals—say university professors—and those in highly educated liberal professions.

The importance of this lies in the ability of those in higher socio-economic classes, i.e. those at the top of the income distribution, to reproduce themselves. Consequently, those at the bottom are placed at a comparative disadvantage. Rudolf Richter (2002) notes that in their analysis of French educational institutions, Bourdieu and his colleagues found that elites reproduce themselves through the control they exercise over institutions. An elite interacts with others among the elite, and through this interaction it

reproduces. *Habitus* in this sense means that the system reproduces itself, because those with power reproduce themselves and thus separate themselves from the masses.

Deeply rooted *habitus* gives rise to all specific tastes in food, clothing, art, and so on. David Gartman (1991) suggests that a bourgeois taste for freedom is defined in opposition to a working-class taste for necessity. The class structure of society, which no doubt can be perpetuated through inequality, becomes embodied in the respective *habitus* of each class because that structure determines the exposure of individuals to different material conditions. As Roy Nash (2003) notes, *habitus* means that social structures arise from the process of socialization, which in turn create a prism through which we view the world. Therefore, if as a result of income inequality different groups are socialized differently, the effect will be for the social structure—unequal ones at that—to reproduce themselves.

Rising income inequality has also had an impact on access to healthcare. The strongest evidence appears to show that those with low levels of income have poorer health than those with higher levels. Nevertheless, income inequality per se is not the main factor affecting health status either in the United States or other countries (Mullahy et al 2004). While there is a strong positive relationship between individual income and individual health, there is less evidence of a relationship between aggregate income and aggregate health (Eibner & Evans 2004).

### **Political Effects of Inequality**

Because income inequality affects resources, the central question is to what extent those without may be inclined to opt out of the political system. A bedrock principle of democratic theory is the notion that all individuals as citizens enjoy the same consideration of their preferences and

interests. All citizens have the same access to governing institutions, and at the most nominal level, this access finds expression in one-person one vote, equality before the law, and equal rights when it comes to speech, press and assembly. Voter turnout, for instance, is much higher among the wealthy than among the poor. But as Sidney Verba et al (2004) note, the participation gap between income groups is even higher among those who take a more active role in electoral politics, whether it be working as a volunteer in a campaign or making campaign contributions. Although the affluent are somewhat more likely to give time to a political campaign than the less well-off, they don't systematically give more time to the poor when they do actually get involved in a campaign. Voter turnout in the United States is lower than elsewhere, in part because it is more difficult to register to vote. But among registered voters, turnout in the U.S. is closer to that in European countries. Some have suggested that this could be remedied through a policy of mandatory voting, as is practiced in some European countries (Lijphart 1997).

The most important individual and contextual factors influencing the extent to which one participates in the political system is the socioeconomic (SES) model of participation, which stresses a strong association between political activities and an individual's income, participation, and especially education. And the single most important source of participation inequality is the cumulative effect of educational differences. Richard Freeman (2004) notes that on a world scale the U.S. ranks 138<sup>th</sup> in turnout among countries holding elections. Cross-country comparisons suggest three reasons for low turnout in the bottom parts of the U.S. distribution. First is the weakness of American trade-unions, and unions usually organize low-income workers to vote. Second, the U.S. has a first-past-the-post two

party system, which elicits smaller turnover than proportional representative systems of voting in which minority opinion votes so as to have a voice in legislation. And third, the congressional-presidential system elicits smaller turnout than a parliamentary system. While the fact that Americans have become more educated, work in high-status occupations, and have higher family income than in the past works to raise turnout, the rising proportion of the adult population who cannot legally vote works to lower turnout. Moreover, increased time constraints on people as a result of work and family commitments may also be a factor in reducing voter turnout.

Ian Shapiro (2003) suggests that it is better to think of democracy as a means of managing power relations so as to minimize domination. The challenge, then, is to devise ways to manage power dimensions of human interaction that limit domination while minimizing interference with non-power dimensions. In modern times democratic control suggests an independent activity that is subjugated to democratic constraint. What differentiates government's activities from those of other social actors involved in activities such as responding to market failure, building infrastructure, providing education, insuring banks, and providing welfare, is the specter of legitimate coercive force. If democracy is about structuring power relations so as to limit domination, it then becomes unnecessary to think of questions about citizenship as different from questions about any other superordinate constraints. At the same time, a conception of democracy predicated on reducing domination must also pay attention to the relationship between the political system, i.e participation, and the distribution of income and wealth. The question of particular concern is whether, and under what conditions, democracy redistributes to the

bottom quintile of the population those who are living — or are in danger of living — in poverty.

Shapiro argues that we have become accustomed to the coexistence of democracy with substantial inequality. And yet Nineteenth century elites initially opposed the expansion of franchise out of fear that the newly enfranchised electorate would exert political pressure to redistribute downward. But there has been no demonstrable relationship between expanding democratic franchise and downward redistribution. Intuitively one might think that the greater the inequality the more likely it is that there will be effective demand for downward redistribution, but the opposite would actually appear to be true. As inequality rises and passes a certain threshold, downward redistribution becomes less likely, which no doubt has something to do with the poor being less likely to participate in the process in the first place. And yet, the more extreme the income inequality, the greater the psychic distance between the haves and the have-nots. Such psychic distance speaks to the anomie that the less affluent are likely to experience out of a sense that because they are distinctly different, the system will simply be unresponsive.

For many contemporary democratic theorists, however, there cannot be real political equality unless there is a measure of economic equality. Unequal distribution of wealth and income may adversely affect individuals' ability to participate in the democratic process on the same footing as equals. Unequal distribution in wealth and income may result in procedural inequality to the extent that those lacking in wealth and income may not enjoy the same access to political and policy officials as those who possess wealth and income may enjoy. With greater concentration of wealth at the top, those at the top are in a better position to use

their wealth toward the attainment of their political and other ideological objectives (Bachrach and Botwinick 1992, pp. 4-5). Unequal distribution in wealth and income, then, results in unequal access. To the extent that this is true, the democratic state cannot possibly be treating its citizens as though they were on an equal footing. Consequently, inequality affects our ability to be free, as unequal distribution will effectively result in some being able to make choices that others cannot. Those with more resources may be better positioned to pursue their goals and objectives, while those with fewer resources may find that their ability to pursue their goals and objectives is limited as a result.

### **Is Income Inequality Really a Problem?**

To the extent that income inequality leads to various social inequalities and distorts the distribution of power in the political realm, it becomes a policy issue that perhaps needs to be addressed. Aside from the obvious material reasons for alleviating abject poverty, it would also appear that steps perhaps need to be taken when there is an obvious threat to the democratic process. Timothy Gaffaney (2000) maintains that a democratic polity operates on the premise that individuals will be politically autonomous—that they indeed will be citizens. A democratic society does not necessarily have to entail economic equality, but it does have to ensure that conditions for participation are available to all individuals, because only when it does so does it guarantee a universal application of citizenship. In fact, the state must guarantee conditions for full citizenship, which might suggest that it has an obligation to pursue those policies that result in a more equitable distribution of income.

Elizabeth Anderson (1999) suggests that equality is about individuals' relations to others. The aim, then, is not to ensure that people necessarily get what they morally

deserve, but to ensure that they are in relations of equality to one another. The point of equality is to in essence ensure that individuals cannot be exploited and oppressed by others. In theory, then, equality prevents one with greater resources from receiving better treatment than the one with less because both are equal in terms of their respective moral worth. According to her conception of “democratic equality,” all law-abiding citizens are entitled to effective access to the social conditions required to maintain their freedom, i.e. their ability to make choices. Therefore, democratic equality seeks to abolish socially created oppression. It views equality as a social relationship. Moreover, individuals are regarded as equals when each accepts the obligation to justify his/her actions according to principles acceptable to others.

Democratic equality, then, does not require the elimination of income inequality once all citizens enjoy a sufficient set of freedoms to function as equals in society. Society does not have to compensate for inferior natural endowments, but it does have to ensure that conditions are such that individuals can function as equals. The state merely needs to pursue those policies and establish a condition necessary to function as equal and autonomous citizens. Citizenship requires more than the functioning as a political agent; it requires participation as an equal in civil society. Although democratic equality does not require the elimination of income inequality per se, it does suggest limits. These limits would be the point at which income could be converted into status inequality. Which is to say, that considerable income inequality could be a threat as it might result in status inequality. But at the same time, policies that limit income inequality, albeit they will never eliminate them altogether, serve to preserve the necessary conditions for the maintenance of equal social relations

among people. Societies prizing real political equality ultimately have to be concerned with growing income inequality.

Still, the question remains with regards to how income inequality could be reduced. Many have noted that countries with more generous welfare provisions do tend to have lower levels of inequality. This would suggest that short of eliminating free markets, the remedy, though by no means perfect, is for an active welfare state that serves to compensate for the failures of the market place, of which income inequality might be one example. More specifically, there is reason to believe that institutions such as unions and wage floors also reduce income inequality, especially if the effect is for incomes of those at the bottom of the distribution to increase at a higher rate relative to those at the top of the distribution (Gottschalk 1997). On the punitive side, inequality could be reduced through higher taxes on the wealthy. This, of course, raises its own political problems. In the end, however, it is important to distinguish between policies that reduce inequality and those that reduce the effects of inequality.

What is clear, as the example of China suggests, is that countries undergoing economic reforms are more likely to see a widening of income inequality. And only if they are prepared to invest in education and the social safety net, as well as having redistributive taxation, may inequality be expected to be reduced (Benjamin et al 2008). Growth in inequality arises from economic transformation, and the ability to constrain that growth is a function of a government's commitment through policy to alleviate the burdens of that transformation.

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## Industrial Districts

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### **Introduction**

The industrial district is a territorial-economic phenomenon whose importance emerged from the debate on the "Italian model of economic development". It was first brought to the attention of scholars and policymakers by Giacomo Becattini (1987, 1989, 2003) and a group of economists at the University of Florence (Dei Ottati 1995; Bellandi 1982). Interest in the organizational formula of the industrial district subsequently extended to other countries, and particularly to the countries focusing on triggering labor-intensive development processes. It is in this light, for instance, that we can explain the interest of scholars from the Max Planck Institut in Jena (Germany) (Brenner 2004; Fornahl & Brenner 2003), who needed to identify potential trajectories of local economic development in areas of eastern Germany, characterized by a relatively abundant workforce and relative scarcity of capital. It should be noted that international interest in the organizational formula of the industrial district was not only due to the success of this formula in modern-day Italy, but also due to the appeal of Michael Porter's approach to production clusters (1990).

Though the organizational formula of the industrial district has become well known as a result of its diffusion in numerous parts of Italy, it is only fair to say that it has been the object of study ever since the time of Alfred Marshall (1891), who was involved in analyzing the localized development and related factors in several British industrial regions. If the Italian economists concerned with deciphering the dynamics of their country's economic development after the Second World War had not taken it up again, however, the concept of industrial district

would very likely have remained virtually unknown.

### **Italian Economic Development**

Given the above considerations, it would clearly be difficult to understand the issue of industrial districts without first tracing a picture of Italy's economic development, with its substantial postwar dualism, but also the new territorial-economic conditions that emerged.

Italy had paid a heavy price in the Second World War. First, there was the destruction caused by the war itself, which had severely damaged its existing heritage of infrastructure in the most developed areas of the country. Second, there was the structural weakness of an economy in which industry played a scarcely relevant part by comparison with agriculture and the traditional service sector activities. Thirdly, there had been a reassuring adoption of protectionist economic policies, which had made Italian enterprises unused to competing on international markets. These protectionist policies enabled a few genuinely industrial-scale enterprises to benefit from a monopolistic situation financed by consumers. The areas where the main Italian industries were concentrated came within the so-called industrial triangle, i.e. between Milan, Turin and Genova. The other regions in the center and north of Italy had very few sizable enterprises and their businesses were mainly traditional artisan type.

After the Second World War, the Italian economy had to take on an entirely new challenge, in the sense that it had to make its way in an open market for which it lacked the necessary institutional or enterprising culture. The liberalist course was practically inescapable, because Italy belonged to the political, strategic and economic system of the Western world. Italy had always been characterized by a very limited availability of raw materials; all the natural products that

had contributed to its industrial development in the past (wood, coal, metal, oil) were lacking in the country's soil and subsoil. The Italian economy could only be developed by exporting commodities with which to pay for essential imported goods and for new industrial activities. In fact, to develop imports demanded a parallel growth in exports and thus a more open approach to international trade.

Naturally enough, Italy tended to opt for international economic exchanges with the countries of Western Europe, for both political and economic reasons. The political reasons stemmed from the pressure exerted by the other Western European countries to establish forms of integration in order to strengthen their economies so as to withstand the military and political pressure of the Soviet Union more effectively.

The various stages in this process of economic integration were characterized, first, by the convertibility of exchange rates between European currencies; secondly, by the birth of the European Coal and Steel Community (ECSC); and thirdly, by the creation of the European Common Market (ECM). Joining the common market marked a real turning point in the evolution of the Italian economy. Italy's economic development benefited first of all from access to fundamental raw materials at exactly the same prices as its principal European partners. Secondly, demand flows coming from member states were generated, giving rise to an export-driven growth process.

### **International Trade and Development**

The grounds for the export-driven growth approach can be found in Keynes's multiplier theory, on the basis of which it is assumed that an economy's development - in the sense of an increase in employment levels - is achievable when there is an increase in aggregate demand, assuming that the

industrial technologies do not change - and one of the components of aggregate demand is naturally represented by foreign demand.

Be that as it may, growth in foreign demand can have various effects on the economies of the countries affected, and it is in this light we must consider Italy's inclusion in the Common Market, which helped to consolidate the new trade flows and focused a significant part of the demand coming from member states on certain types of Italian production. So the inclusion of the Italian economy in the European economy determined a growth in the demand for Italian goods (and particularly for goods whose production is labor-intensive) especially from the German and French markets. It is important not to forget that, among all the countries adhering to the Common Market, Italy was the one comparatively richer in labor and poorer in capital. Thus, according to the Ricardian theory of comparative costs, Italy could only specialize in mature, highly labor-intensive types of manufacturing that could be carried out in enterprises of small dimensions. Heterogeneous levels of development in Italy, and particularly between north and south, as a result became more accentuated.

At the same time, the economic role of what has been called the "Third Italy" (Bagnasco 1977)—i.e. regions such as the Veneto, Friuli-Venezia Giulia, Emilia-Romagna, Tuscany, the Marche and Umbria—became apparent. These regions have characteristically developed systems of small and medium enterprises specializing mainly in mature sectors and proving capable of achieving good export performances, starting with the markets of the ECM. In the relationship between international trade and growth, we can identify two parts which inevitably overlap. The first part concerns the types of sectoral specializations evolving in the Italian economy. The second concerns the

types of geographical areas in which enterprises in specialized sectors were concentrated.

At the beginning of the European economic integration process, there were really very few Italian enterprises capable of exporting, and they were mainly the larger size industries, so the products that Italy was exporting were of intermediate technological content. This type of specialization began to experience a crisis in 1973-74, under the effects of an oil crisis that forced the enterprises to become more energy-efficient. At the same time, the fallout of the computer revolution was beginning to make itself felt and naturally affected the very logic of industrial organization. Italy consequently further accentuated her tendency to specialize in the mature sectors dominated by small enterprises capable of achieving a significant export performance.

### **Other Experiences Around the World**

Although the study of industrial districts was incubated in the context of the Italian experience, it must also be said that there are quite a few significant experiences elsewhere in the world. The creation of clusters or systems of small and medium enterprises in certain other parts of the world seems to derive from the spreading effects of globalization. In a sense, economic globalization and the consolidation of the web society are creating a space for flows (Castells, 1989) with local network systems as their "nodes".

These local systems form part of more extensive networks, and are in turn composed of networks of small and medium enterprises, so the organization of the entire world meta-system can be seen as an enormous "fractal" form. The diffusion of clusters of small and medium enterprises on a worldwide level thus seems to be the outcome of processes stimulated by three forces that complement

one another. The first has to do with the effects of international trade and a consequent delocalization of many mature manufacturing sectors from the economically more advanced to the less advanced countries; the second stems from the spread of flexible production technologies on a planetary scale; and the third derives from the self-organized capacity of labor that takes effect in territorially restricted areas. It is the combination of these three forces, for instance, that has led to the creation of significant industrial clusters in Asia, particularly in China and India, but also in Vietnam and Taiwan.

Leaving aside the specific development trajectories, in Southeast Asia, the establishment of local systems of small enterprises has been facilitated by the cultural traditions, and family-based structures. In India the Bangalore area has become well-known as the Indian Silicon valley, where thousands of people work in activities relating to information science. Rotating around an important university campus. Of course, there are also areas where small enterprises specialize in traditional manufacturing processes. In China, since the reforms completed at the end of the Seventies, there has been an impetuous growth in the country's economy, a growth in which the development of family-scale enterprises has had a considerable importance. Several industrial districts have sprung up in the Jinjiang area, revealing characteristics entirely similar to those seen in Italy (Zheng, 1995), specializing in the ceramics, footwear and clothing sectors.

In the United States it is difficult to speak specifically of industrial districts, whereas reference is generally made to the concept of "clusters", with which Porter (1990) meant to indicate vast agglomeration of enterprises in a relatively bounded territorial context, not necessarily belonging to the same industrial sectors and not necessarily all small in scale.

Paradoxically (because it is not specialized in mature production processes), a cluster that most resembles the industrial district is Silicon Valley, with its numerous enterprises operating in the field of computer science and related sectors. In fact, the Silicon Valley enterprises work as a system and rely on the role of a shared culture (Rosenfeld, 1996). Another interesting cases considered by Rosenfeld (1996) is the furniture district in Tupelo, in the northeast of the state of Mississippi, where a furniture industry first settled, giving rise to generations of workers, some of whom founded their independent enterprises. The local government in Tupelo facilitated the settlement of other enterprises in the sector and supported the enterprises in the district by organizing schemes and providing infrastructures, while the local university created design courses and a materials research center.

Another case of industrial in the USA is the knitwear district in Catawba, in North Carolina. Already in the early 20<sup>th</sup> century, there were several enterprises operating in the sector, soon joined by entrepreneurs arriving from outside in search of low-cost labor. Today, the district has more than 300 companies with 20,000 employees. The local enterprises have created a lively association that has created a technology center together with the local college and with support from the local government.

On the other hand, if we look at a country of consolidated industrial tradition, such as Germany, we find no significant cases of industrial district (Glassmann and Voelzkow, 2001). If anything, there are important area-systems, where large-scale enterprises operate, prompting the birth of complementary enterprises. The German industrial clusters developed due more to the effects of economic-industrial forces than the

social and cultural forces, unlike the case of the Italian industrial districts.

Another European country with solid industrial traditions governed by its own peculiar industrial policy is France, where the state has always occupied a fundamental role, governing and influencing the development of the country's industry with a strong inclination for state intervention and centralization. In this type of setting, small enterprises have been granted scarce attention and the French experiences of systems of small enterprises and their local governance are hardly comparable with those of Italy (Ganne 1990). Moreover, there has been no sign of any decline in the role of the metropolitan area of Paris, where the country's principal enterprises have concentrated their decisional centers, confining the other cities to a marginal role.

### **Porter's Dynamic Approach**

A first hypothesis for analyzing the reasons why groups, or clusters, of Italian small-to-medium enterprises succeeded in obtaining significant commercial results on foreign markets could be the strictly classical hypothesis relating to the endowment of production factors. To tell the truth, this is an entirely static theory that fails to consider why the enterprises of a certain geographical areas succeed where similar enterprises in another geographical area fail. In fact, such an approach is static because it is based on the role of the endowment of factors after discounting any innovative or other processes. A more useful analytical method may lie in the work done by Michael Porter (1990), which has a distinctly more dynamic basis. In fact, Porter's work appears dynamic because it considers a set of interrelated and changeable factors, and the enterprising strategies used to exploit or maybe even change these factors. In other words, the view of the competitive process evoked by the

notion of competitive advantage is fundamentally dynamic since it is the outcome of jointly applying a great variety of forces that interact and vary with time. So the factors coming to bear on the potential competitiveness levels of a country and/or specialized area (or industrial district) are numerous and interrelated, and they are also influenced by exogenous forces.

Porter clearly focuses on the role of innovation and change, and it is change - i.e. the ability of enterprises to adapt to the outside environment, or the capacity to anticipate forms of emerging structures - that act as the keystone to competitive advantage conceived in a dynamic sense. This applies particularly to enterprises operating on the international market. In fact, operating on the international market becomes a prerequisite for industrial development, if nothing else because it increases the competitive dimensions in which enterprises operate. Competition at international level provides local systems of enterprises with the stimulus to improve, i.e. with a set of information that is generated both inside and outside such local systems of enterprises and that can be translated into innovation in processes or products, and/or into reductions in production costs. Such innovation can subsequently be facilitated by the existence of strong competition at local level, which drives businesses to make the best possible use of innovation within these production systems or clusters. This explains why it is important to have areas with a strong concentration of enterprises, because where the enterprises are few and far between, or in a monopolistic position, the force driving innovation may be considerably weakened.

### **Becattini's Definition**

As we said earlier, the first person to draw the attention of the economists to the industrial district as a way to organize production was

Alfred Marshall, who said that production efficiency could be achieved by bringing numerous small enterprises together in a limited area providing the production conditions of the sector concerned were suitable. By production conditions, we mean the existence of linear and homogeneous production functions, in the sense that any increase in production is linearly functional, but not more than proportionally functional, to an increase in the production factors. In such cases, there are no "scale economies" at work (which, in other production contexts, make the larger size enterprise more competitive), so the small enterprises have just the same marginal productivity of the factors as the larger enterprises. Meanwhile, it is worth noting that combining a number of small enterprises generates "external economies" deriving from a given enterprise being able to use the services of other territorially local enterprises. Always assuming that there are sectors characterized by linear and homogeneous production functions (the majority of which are mature sectors), we can see that creating clusters of small enterprises specializing in one type of production in a territorially bounded space exposes these enterprises to the maximum competition. But their small size does not harm their production efficiency, while their greater numerosity improves their levels of production efficiency, thanks to the stronger competition.

Another aspect to consider is that a district contains not only the enterprises that actually manufacture the product characterizing the district, but also businesses that produce complementary goods and services. These are what Porter calls "support sectors" and they represent a necessary integration of the basic production processes. An industrial district therefore consists of numerous small enterprises that make the same product, or varieties of the same product, plus numerous

businesses that provide complementary goods and services.

As mentioned at the beginning, the concept of industrial district in the sense used by Marshall was relaunched by Giacomo Becattini, who first focused on analyzing the characteristics of Tuscany's economic development. Becattini made the point that, in the years of postwar reconstruction, Tuscany's industrial growth was mainly thanks to the expansion of local systems of small enterprises. These systems were characterized by their being sectorally specialized and territorially concentrated. The typical district was certainly the one in Prato, which specialized in manufacturing wool. Studying the Prato industrial district and the organizational forms that took hold in Prato enabled Becattini to come up with the following definition of industrial district, intended in the sense used by Marshall:

I define the industrial district as a socioterritorial entity which is characterised by the active presence of both a community of people and a population of firms in one naturally and historically bounded area. ... In the district – and unlike in other environments, such as the manufacturing town – the community and the firms tend, as it were, to merge. (Becattini 2004:19)

Numerous areas are characterised by a sectoral specialization: these include tourist areas, for instance, where much of the active population is employed in the tourist sector and in tourism-related activities; but this does not make us speak of "tourist districts". If anything, we might talk of "specialized economic regions". Basically, from a point of view of its definition, the industrial district has its own specificity and the term "district" must not be confused with that of "economic region". Industrial districts are characterised

by different elements that will now be examined in more detail.

### **Competition and Cooperation**

The term "population of enterprises" is used to mean not a random set of enterprises, but a group of businesses that interrelate with one another. They may be links on the supply side (and consequently of cooperative type), or they may derive from the fact that many enterprises produce the same or similar goods (competitive links). Many enterprises consequently specialize in one or more stages of the production process involved in the district's industrial sector, which includes both the enterprises that manufacture the goods characteristic of the industrial district and the enterprises that provide complementary goods and services.

From what we have said about the form of the production functions, we can see that the district expands by increasing the number of enterprises rather than by increasing the dimensions of one or a few enterprises. What happens is a progressive division of the work involved with a consequent progressive specialization of the enterprises. Lastly, there is a growth in the number and variety of the complementary or support enterprises too. In a sense, an industrial district represents an economic ecological system, where one species (the enterprises operating in or supporting the sector characterizing the district) conquers the area and acquires a leadership. In this ecological system, the enterprises improve their industrial performance due to competitive (and cooperative) mechanisms that govern the nature of the relations between the enterprises.

To analyze the competitive mechanisms, we need to move into the realm of abstraction. We must imagine, first of all, that all the enterprises operate in or support the district's characteristic sector; secondly, that



all the enterprises are small; thirdly, that the enterprises do business as buyers and/or suppliers; and fourthly, that their relations are of a competitive and/or cooperative nature. Structuring the industrial district in this way leads to the creation of a close-knit mesh of economic relations that relies on an equally close-knit network of social relations.

The competition among the enterprises producing the same or very similar goods constantly obliges them to improve their production efficiency levels and to introduce innovation. The enterprises become specialized because it is only way they can stay small and achieve high levels of efficiency. Specialization makes them gain in technical competence, both in the production processes they use and in the goods they manufacture. This competence is furthered by competition with the other enterprises in the district. In addition to competing, the enterprises also cooperate with one another. There are basically two forms of cooperation: one involves the cooperation between the enterprises that manufacture a given product and the enterprises that make the necessary machine tools, or the correlated semiprocessed parts. Strong co-operative links are generally established between the enterprises that use and the enterprises that provide the production machinery, with exchanges of opinion, agreements concerning the introduction and testing of innovation, and so on. The nearness of local suppliers also enables a constant sharing of experience, as well as the preparation of experiments jointly conducted by the producers and the users of the machinery. For the machine tools manufacturers, the industrial district is a sort of living laboratory where they can conduct experiments that can produce excellent results.

Another form of cooperation is established between buyer enterprises and supplier enterprises within the district. Here again, the

two types of enterprise share their experience and often work together to identify the best solutions for specific technical or commercial problems.

A third form of cooperation is sometimes created between enterprises even though they are in competition with one another. There are business areas that may be beyond the reach of a single small company: suffice it to mention the penetration into a foreign market, or attendance at particularly important trade fairs, or particularly costly innovations. On their own, none of the small enterprises in the industrial district can shoulder the costs and risks of such action, but if they join forces they can. But how do they come together? Very often the factor that enables a cooperative behavior of this nature to be undertaken is the presence of industrial associations of which the enterprises are generally members. Such associations, stimulated by a few of the more dynamic enterprises, can promote schemes such as participation at an international trade fair, collecting any public funds, identifying expert consultants and providing logistic support.

### **Knowledge, Loyalty and Trust**

It is easy to imagine that an export pool, or employee training, or technological innovation are more likely to come about where enterprises have the same knowledge of the technical aspects of the problems they have to deal with, and a shared understanding of how potential members of the group are likely to behave.

As concerns their knowledge, it is usually claimed that the enterprises of an industrial district share a general understanding of the technical procedures and trading rules because people born and brought up in an industrial district "breathe" a certain atmosphere right from their childhood; at home they hear talk of problems relating to the life of companies typical of the industrial

district, their friends have members of their families who work in enterprises in the district's characteristic sector, and so on. Moreover, when young people join a (presumably small) company, they rapidly learn all the secrets of the production system and refine their understanding of the problems of that particular market. So we might say that the people and the enterprises living and working in a given industrial district have a common knowledge of the various issues relating to the production and sale of the product typical of their district. This knowledge is largely "tacit", in the sense that it is handed on from one person to another without any explicit, coded procedures.

Sharing knowledge and values can help to reinforce a loyal behavior between the members of the group. Generally speaking, we can say that an enterprise is loyal when it keeps to the agreements it has made with other enterprises, be they customers or suppliers. Such agreements are not necessarily formally defined. They may be informal arrangements based on implicit rules that apply to a certain area, everyone being safe in the knowledge that the other parties will adhere to them loyally. People operating in an industrial district know what type of behavior to expect from the other people in their district and this knowledge makes them more confident (Mistri 2006).

It is important to consider that strong competition between enterprises also tends to make them adopt a loyal behavior. For instance, a supplier enterprise knows well that if it fails to behave loyally, its buyer enterprise will soon find another supplier enterprise in the district to take its place. All the buyer enterprises of an industrial district can therefore reasonably expect their suppliers in the district to behave loyally, so they do not have to resort to costly legal contracts or equally costly control measures.

This expectation concerning the "necessity" of a loyal behavior can be defined as *trust*.

A supplier enterprise might be a little late in delivering the goods it has been asked to produce, or it might use materials that are not entirely compliant with the specifications, or it might finish the products to a slightly inferior level than was requested: such shortcomings do not necessarily mean a breach of contract, but they do give rise to complaints and misunderstandings. Such problems carry costs and such costs sometimes stem not from any lack of goodwill on the part of the parties to the transaction, but rather on a certain ambiguity in defining the details of their agreement. Enterprises have to try to predict every event and measure every quality parameter. All this entails costs to collect information, translate qualitative elements into quantitative parameters, and prepare contracts. Such costs are generally known as transaction costs (Williamson 1979)

If, in a community of enterprises, all the enterprises behave loyally and undertake to achieve the maximum possible levels of diligence, the transaction costs are low, or even nonexistent. For the previously-mentioned reasons, we can assume that the transaction costs in an industrial district are minimal, or at least than the costs of defining the contracts needed in other territorial contexts.

### **Local Community and Governance**

What we have said about the behavior of enterprises can also be extended to the behavior of people. An industrial district is also a community of people who share the same values, with a heritage of behavior patterns that represent what we might call *communicative competence*. In fact, what characterizes a community is the fact that its members have a heritage of symbolic language, i.e. they can produce and

understand messages that enable them to interact with other members of the same community with a minimum risk of misunderstanding. Of course, the signs that can be identified in a working community include those relating to trade relations and labor relations.

Communicative competence applies not only to the people who have an economic role, but also to those who have a public, institutional role, partly because these people are members of the society called upon to govern the community at any given time. In fact, the sharing of values makes the industrial district a more integrated society and thus makes it easier to achieve shared goals and the debate on the reasons for the competitive advantage of the industrial district has pinpointed the importance of taking an approach that seeks the reasons for the local industrial development especially within the logic of social and cultural self-regulatory methods.

There are certainly numerous factors that have played a positive and propulsive part in the development of local systems of small enterprises, but they all stem from locally-rooted industrial and social relations. That is why, in the situation to which we refer here, the interaction between the industries and the action taken by local organizations has an essential role, because the latter are asked to contribute towards and support the growth of the so-called "districtualized" economies. This informal goal can be achieved either by ensuring the maximum harmony between private and public values, or by ensuring the administration of the infrastructural services that are important for the purpose of reducing the transaction costs and reinforcing the outside economies.

It is a commonly-held opinion that the action of local organizations is an important part of the factors of competitive advantage (Messina 2001). Effectively consolidating the

existing and operating relations helps the industrial district to cope with the new forms acquired by market relations, now that the traditional factors of competitive advantage are under strong pressure, especially in the emerging system of international economic relations. Evaluating the nature of the relations between the real economic system and the local organizations in the context of an industrial district makes us see how the industrial district's development is, to some degree, conditioned by the choices, attitudes and culture of governance of the local economy that these local organizations succeed in expressing. In fact, their programming action and measures soon take effect on the enterprises operating in the area, on which the local organizations have a power of economic direction and consequently of orientation, prohibition and support.

Returning to the fundamental picture that Becattini painted of the industrial district, we can emphasize the role of the environment as a whole and thus of the general involvement of the local community. There is an continuous interaction between economic activity and social culture (and the consequent system of socially shared local values), in the sense of a set of economic, social and cultural variables that influence the characteristics of the industrial and social structures, interpersonal relations and dealings between enterprises. So it is culture that acts as a bond for social and economic interactions at local level. Social exchange seems to be assured by the existence of elements of cultural and even ideological cohesion, by the acceptance of a common economic and social outlook. The district thus becomes a "communitarian market" in the sense used by Dei Ottati (1995). A significant aspect of the social basis for the industrial district lies in all the social groups sharing a common universe of values despite the

legitimate differences of political opinion. First of all, the cultural distance between entrepreneurs and employees in an industrial district is lower than in areas dominated by large-scale enterprises: in large businesses, the technological, commercial and financial know-how lies exclusively in the hands of a few, whereas in the industrial districts this type of competence is more widespread, so no baseline social and/or cultural barriers are created and there is a greater chance of social circulation within the district.

Social cohesion involves identifying the district's general objectives, and even its politicians come from an environment steeped in a common industrial and economic culture, with a very thorough understanding of the problems and expectations of the economic and social agents of their area. The enterprises' development objectives are ultimately seen as the objectives of the local areas and communities and the shared culture and enormously accentuated physical nearness make the local administrators necessarily become the spokesmen for the development needs of societies that would be unable to understand or accept a show of indifference to their economic demands.

## **Conclusion**

Following the above considerations, it seems that Marshall's district formula is essentially a feature of Italy, although there are similar experiences in other countries. If we expand our horizons to a more global context, we can see that the district formula has several of the features of the looser formula illustrated so well by Porter (1990) and formalized by Brenner (2004). However, bluntly put, a fundamental difference between Porter's clusters and Marshall's districts can be seen in the fact that industrial districts are groups of enterprises operating essentially in mature industrial sectors, whereas clusters may also consist of enterprises operating in high-

technology sectors (Simmie 1997). What the two organizational formulas have in common is the reticular nature of the relationships between enterprises (Gilly & Torre 2000) and between people (McNaughton 2000).

More than a few governments are seeking to facilitate the formation of industrial clusters, furthering cooperation between enterprises, universities and local authorities. These efforts generally focus on creating technological clusters, where it is assumed that the transfer of know-how from research centers to enterprises, and from one enterprise to another can take place more easily if the conditions are right for local collective goods to develop. Trust and the exchange of information are certainly important local collective goods and there is a general conviction that the administrative authorities should facilitate the creation of these local collective goods (Staber 1996).

It is worth noting, however, that involving the administrative authorities is not the only option available; methods entailing the enterprises establishing their own relationships and developing their capacity to generate independent collective organizations also have an important role. It is therefore legitimate to speak of an "approach to governance": governance is basically a term used to indicate the specific ways in which private or public institutions and organizations coordinate and regulate the actions and transactions between the subjects acting within an economic system (Hollingsworth & Boyer 1997).

Effective governance relies largely on the existence of three elements: (1) a consolidated "social capital" (Lin 2001:), (2) the formation of an adequate enterprising spirit, and (3) a political culture in favor of enterprising spirit. For instance, where there is no strongly-developed sense of civic responsibility, there is likely to be a strong propensity for corruption in public office, and

this generates distrust on the part of potential entrepreneurs. It is not always possible to transfer the Italian industrial district formula to countries where the basic social and political conditions it requires are lacking, as is often the case of countries in the Third World. It is hardly surprising that the sub-Saharan African countries have so far been unable to develop industrial districts along Marshall's lines, while other significant experiences have been able to emerge in the Far East, as discussed earlier.

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### **Introduction**

State intervention in the economy can take a variety of forms. Firstly, the state can have a minimal role in market processes, which neoclassical economists favor. In this case, there is limited need for state intervention. The state is inactive in terms of market outcomes, except in cases of market failure; the prevailing view holds government to the basic roles defined for example by Adam Smith, and others. Thus, the market functions freely. Secondly, state intervention can be in the form of industry policy designed to assist enterprises in confronting competitive forces mainly through the provision of information, tax concessions, and tariff protection. Industry policy also encourages enterprises indirectly, through offering market incentives, to reach a market outcome that is socially desirable. Thirdly, state intervention can be through the imposition and enforcement of regulations, which restricts enterprise choice. Here we are concerned only with industry policy.

Industry policy includes all actions taken to promote industrial development beyond that permitted by a free market. Rasmussen et. al. (1983:752) points out that the term industry policy has come to capture and describe every action that might stimulate industrial development, and thus economic growth. Houghton et. al. (2000:5) argued that there are many different definitions of industry policy provided in the literature, each implying a somewhat different scope. Some include in industry policy all actions directed at improving the long term performance of the economy, whereas others link industry policy to a certain class of interventions or to interventions designed to correct specific cases of market failure.

Generally, industry policy is interpreted as covering policies, strategies, and initiatives directed at influencing the structure and long term performance of an industry, in the context of long term global trends. Industry policy can influence the long term structure and performance of the economy, provided that it is carefully specified and implemented, and that it makes use of market forces as far as it is possible; “industrial policies in East Asia and Europe were never *anti-market*. Their industrial policies involved the selective control of market forces. The control of market forces was designed to enhance the ability of national firms to compete in the world market” (Chang & Grabel 2004:11; original emphasis).

Public infrastructure, human capital investment, training of workers, and research and development (R&D) are activities that have been included in industry policy. Such policy focuses mainly on issues of increasing productivity, competitiveness, spurring technological advance, and revitalizing distressed industries. The government offers incentives (i.e., subsidized loans, loan guarantees, industrial revenue bonds, tax incentives, etc.) in order to increase the rate of return on investments. By and large industry policy can be formulated on several levels including an industry level, a regional level, a bilateral level, and a level according to company ownership.

Industry policy can have two elements: functional interventions and selective interventions. The former, which neoclassical economists favor, are those interventions that remedy market failure without favoring any specific sector over another. The latter are policies designed to favor individual activities or groups of activities in order to correct sub-optimal resource allocation, in a static or a dynamic sense. Liberal interventionists and market socialists favor selective interventions in industry policy. Liberal interventionists

argue that industry policy is essential given the inability of the market system to “pick winners”. Whereas market socialists argue that industry policy and regulation is totally ineffective in a capitalist system because the state does not have the power to enforce its decisions. Under such system, power resides with the owners of capital whom resist any attempt to influence their decision-making process, especially if these decisions contradict their goals such as profit maximization. Consequently, in order to succeed, based on the market socialist point of view, state intervention and in our case industry policy, which uses social benefits as a yardstick requires the elimination of the sources of power in a capitalist system; that is, private property. The market socialists argue that this can only be achieved in a socialist system, which is dominated by social property.

### **Types of Industry Policy**

Comparative advantage theory of international trade (Ricardo 1817) was developed in a specific historical period when natural resource endowments and capital-labor ratios determined economic location. The theory of comparative advantage is based on unrealistic assumptions, especially for today’s world, about technology, industrial structure, macroeconomic conditions, and the mobility of labor and capital (Chang and Grabel 2004:60). In consequence, “the ‘old’ comparative advantages based on inputs and low cost workforce start to fade away” (Zanatta & Queiroz 2007:423). Currently, this has been replaced by an era of knowledge-intensive industries where comparative advantage is socially constructed rather than created naturally and historically. Natural resources have ceased to dominate economic activity. Long-run economic growth is the result not only of a country’s resource endowments, but also of its capacity to satisfy

both domestic and foreign demand for knowledge-intensive production processes. Should a country fail to adequately develop such processes, the result is marginalization from lucrative trade relationships and resulting stagnation. The inability to exploit opportunity cost given the lack of demand for specialized goods means that comparative advantage fails. The presence of high and persistent unemployment and very large transaction costs contradict the assumptions of comparative advantage (Thurow 1996:215, 217). Hence comparative advantage is irrelevant. Industry policy should facilitate strategic economic advantage. In addition, market actors tend to underestimate the long-term gains of investment, especially R&D, also markets are not able to value externalities correctly, coordinate large interdependent decisions, and avoid duplicate investments justifying in this way the need for industry policy (Chang & Grabel 2004:74).

Industry policy emphasizes the cooperation between government, banks, private enterprises, and employees to strengthen the national economy. Industry policies in advanced economies have focused mainly on the improvement of firm performance through addressing market failures, expanding technological capabilities, and paying greater attention to the quality of investment and human resources (UNIDO 1995). In developing and transition economies, industry policies have focused on market reforms, privatization, and increasing the private sector. Industry policy in the same countries also favored absorption and attraction of technology, internationalization of production, openness of the country (as this is measured by the ratios FDI/GDP and trade/GDP), and, the increase of competitiveness in the economy.

Industry policy can also take the form of assistance in the development of export



oriented enterprises when the government is offering export subsidies, R&D subsidies, or lower taxation rates (Barros and Nilssen, 1999). Thus, industry policy can be part of: (1) the a liberalization trade program; (2) the a re-orientation of the trade; and (3) a scheme to attract foreign multinational enterprises (MNEs). Moreover, possible industry policy objectives can be the creation and promotion of new technology-based firms and research within enterprises that emphasize collaboration between companies, and collaboration between companies and universities. It may also include the employment of young researchers, the creation of research groups with personnel drawn from industry, universities, and research institutes, the diffusion and technology transfer policies, and infrastructural and innovation policies (Rolfo & Calabrese 2003:254-5).

Industry policy can take the form of “picking winners,” in which the government promotes industrial development by selecting specific investment projects or enterprises for financial and technical support. This form of industrial strategy is based on the belief that the government is more effective than private investors and the market at selecting projects likely to succeed in promoting economic growth.

Critics argue that industry policy in this form is likely to result in government support for projects that would have been adopted anyway, so there is no need for assistance or that the project without assistance would have been unsuccessful in any case. Moreover, critics claim that it is better for governments to concentrate on providing non-discretionary policies, such as education to produce a skilled labor force, promoting efficient capital markets, and permitting private businesses to decide the most profitable projects which through the “invisible hand” also stimulate economic development and growth.

Derashid et. al. (2003:46,48-9) points out the issue of discrimination in government industry policy, as benefits may be given only to strategic or large firms in specific sectors, such as manufacturing or tourism, in order to promote both economic and social goals including: protecting domestic sectors from foreign competition, increasing exports, enhancing efficiency or competitiveness, and fostering high-tech development. However, as a result of this discriminatory policy selected firms and sectors are in a good position to influence and lobby the government for favorable treatment. The concept of “behavioral additionality” is relevant in this context: the provision of financial assistance is likely to result in a change in strategy/behavior by firms vis-à-vis preceding government intervention. Thus, government intervention in the form of industry policy can have predicted and unpredicted positive/negative externalities linked with the change in strategy/behavior by firms (Leniham et al 2007:318).

Industry policy can also be justified based on the infant industry argument. As a new industry or enterprise in its early stages of its development is unable to compete effectively with the lower prices and higher quality of goods of present producers, especially foreign producers, some short-term protection is necessary. It takes time for an industry to operate at a minimum cost of production until it has reached a sufficient size to obtain significant economies of scale. Protectionism will allow the infant industry to grow and develop to the point at which it can compete on the international market without protectionist measures. In this case, governments are often inclined to support the development of new industries either by subsidies or by trade controls, but usually with protective tariffs. State support for infant industries is also justified if there are external benefits, such as the creation of new skills

which can then be exploited by other industries. Thus, nurturing infant industries with protection is necessary until the industry has reached an optimum size.

Critics of the infant industry argument claim that it is not proper for governments to support infant industries. They argue that infant industries are, by definition, those that are not competitive enough to survive and therefore end up dependent on the government and its protection in order to continue existing. It is also impossible for governments to determine which industries have growth potential. Concerns associated with the small scale, lack of production experience, and lack of market reputation are part of the necessary evolution and development of new industries. New firms should not be initiated as long as the long-run profits are expected to be sufficient to repay costs. An infant industry tariff raises the price of consumer goods, thus reducing market growth. In the end, while protection is supposed to be only short-term the industry becomes complaisant and in the long-run political pressure maintains the inefficient tariffs.

### **Industry Policy in Practice**

Nearly all of the developed countries in the 2000s used industry policy to rebuild their economies after WWII, such as Japan, France, Norway, Austria, and Finland. Even the USA uses industry policy without been identified as such (Chang & Grabel 2004:10-1). The development of transistors, radar, computers, nuclear fusion, laser technology, and the internet were made possible by direct defense subsidies by the federal government of the USA (Chang & Grabel 2004:11).

Undertaking industrial policy evaluation requires examining good-practice international studies in terms of developing appropriate methodologies; nevertheless, identifying the best practice in evaluating

industry policy is methodologically an extremely challenging task (Leniham, et. al., 2007, p.313). While most policy evaluation approaches currently adopt methods combining quantitative and qualitative techniques, these methods still lack the ability to attend to the complex cognitive issues implied by the possibility that not all policy decisions are rational (Ramsey & Bond 2007:415). The design, monitoring, and evaluation of industry policy require a competent civil service which is not necessarily available in developing countries (Chang & Grabel 2004:79).

The Commission of the European Communities (CEC) (2002:3) mentions that industrial policy in the European Union is horizontal in nature and aims at securing a framework of conditions favorable to industrial competitiveness. An horizontal industrial policy has to take into account the specific needs and characteristics of individual sectors. The regulatory-framework and business environment in which firms operate are highly sector-specific. Hence, to be effective industrial policy needs to be applied in response to the particular needs of every sector.

According to the CEC (2002:2) competitiveness is the ability of the economy to provide the population with high and rising standards of living and high rates of employment on a sustainable basis. Industrial competitiveness depends on policies such as competition, the internal market, research and development, education, trade, and sustainable development.

Industry policy aims to provide a framework of conditions in which entrepreneurs and businesses can take the initiative, exploit their ideas, and build on their opportunities. However, industry policy needs to take into account the specific needs and characteristics of individual sectors. Therefore, industry policy needs to be applied

differently, according to the specific sector. For example, many products, such as pharmaceuticals, chemicals, automobiles, are subject to detailed regulations based on their inherent characteristics and/or based on their use.

The CEC (2002) also maintains that industrial competitiveness deserves particular attention to three areas—knowledge, innovation, and entrepreneurship—and concluded that industrial policy inevitably brings together these elements on a horizontal basis in a form of sectoral applications.

The industrial policy of the European Union has a key goal to set out the boundaries within which industry and entrepreneurs can pursue their ambitions (CEC 2002:31). It aims to establish a predictable legal framework which can be adapted in response to policy needs and to ensure that the conditions are present for industry to develop and to realize its competitive potential. European society, as the CEC states, cannot be passive in its attitude to their source of wealth. The availability of technology, skills, an educated workforce, a positive attitude toward risk-takers, finance, and the other conditions which form a truly competitive and innovative business environment have to be the active policy concern of the policymakers. Industry policy also ensures the institutional framework and instruments necessary for the business environment and for industry to be able to function efficiently and to act in accordance with its public obligations. In the end, the CEC points out that enlargement will be a major source of opportunities for industries in both its new and existing Member States, and thus should make a positive contribution to overall industrial competitiveness.

The enlargement of the EU offers important opportunities to European business, not only as a result of the extension of the internal market, but also because it offers the

possibility of reorganizing value chains across the continent, making the most of the competitive advantages of the New Member States. Nevertheless, the CEC (2004:2) concludes that for these countries, the benefits of their relatively low labor costs will be temporary. The transition to a knowledge economy is vital and a certain regulatory prudence is necessary to avoid putting a strain on the industrial competitiveness of these New Members.

The CEC also suggests that the European Union must continue to develop the sectoral dimension of industrial policy. This implies analyzing, at a sectoral level, the effectiveness of policy instruments which are horizontal in nature, with a view to evaluating their relevance and to propose, if necessary, the appropriate adjustments. The combination of the activities was announced in the Communication report of 2004 established between the European Union countries and the European Commission (CEC 2004).

This Communication report should assist Europe's industry, especially in the new Member States, to successfully meet the challenges of structural change and to contribute, therefore, to meeting the objectives the European Union set itself at the Lisbon European Council. The Lisbon Strategy was developed due to the fact that economic performance in the EU was lagging behind the USA. The argument was that the EU's social model had become obsolete and inflexible, requiring reform to decrease unemployment and increase competitiveness. Targets were set at 3% growth per annum and 70% employment rates throughout the EU by 2010 (Bailey et al 1997:455). This communication presents sectoral initiatives already set in motion in sectors such as the automobile industry and mechanical engineering.

Industry policy experience in the UK reveals that the objectives were to promote

enterprise innovation, increase competition, safeguard or expand employment, modernize technology, improve infrastructure, produce new products, introduce new production processes, and to increase labor productivity, job creation, and firm efficiency. Industry policy had the goal to directly improve the economic performance of assisted plants of regional economies by offering discretionary or non-discretionary grants, subsidies, and support schemes. With industry policy, the UK government was trying to maximize social welfare, better allocate and more effectively use natural resources, explore the country's competitive advantages, and finally, increase GDP and economic performance (Harris and Robinson 2004:528-9).

In the case of Italy, industry policy mainly takes the form of regional industrial policy that encourages companies to purchase new machinery and equipment which enhances innovation. Thus, in this case, industry policies support competitiveness, promote infrastructure and services, and aid territorial areas, industrial districts, and areas of re-industrialization (Rolfo & Calabrese 2003:259).

The link between industrial policies and industrial restructuring during the transition period can be demonstrated by Slovenia's successful transition. Bartlett (2000:11) stated that "Slovenia required an equally strong commitment to industrial restructuring and the introduction of industrial policies, which would be capable of facilitating the transition to a market economy". Slovenia faced the need for widespread industrial restructuring after 1991, in the form of internal restructuring of enterprises, re-orientation of trade, improving quality and management efficiency, encouraging the entrance of new private firms, and expanding small-scale enterprises in order to satisfy the demand from the new trade partners of more advanced economies. Specific Slovenian industrial

sectors (i.e., textile, steel, basic iron, metal, wood, and furniture products) were incorporated within an industry policy which was the main target of special assistance programs funded under the EU PHARE economic assistance program. Bartlett (2000) concluded that the Slovenian industry had to become internationally competitive, to be privatized, restructured through the cancellation of debts, and export oriented. In addition, industry policy had to enhance the creation of new private businesses, both local and foreign by providing support through funds from the EU. The ultimate goal was economic integration and EU accession, which actually was achieved at 1 May 2004. Hence, industry policies in transition countries had to involve tax subsidies, employment subsidies, cancellation of bad or non-performing loans, government-sponsored investments in private firms, and initiatives for Small and Medium Enterprises (SMEs), and lower taxation rates (Bartlett 2000:19-20).

Industry policy in Asia took place when access to basic infrastructure was liberalized in the name of national or supranational market competitiveness, e.g. Singapore, China, India, and Japan (Lovelock et al, 2000, p.278). In Japan, the powerful Ministry of International Trade and Industry (MITI) has often taken an active role in the development of major industries, particularly electronics and software. The impact of this intervention is disputed, given that Japan is still not a powerbroker in software, and has lost much of its advanced electronics industry to the Asian Tigers, especially South Korea and Taiwan.

In Malaysia there is an explicit industry policy that includes various incentives, such as tax benefits (Derashid et al, 2003, p.46). Malaysian governments are attempting to diversify the economy and industrialize the country with the help of an industry policy

aimed at the development of the manufacturing sector and a shift from an import substitution to an export orientated industrialization strategy. This industrial policy provides a large number of investment incentives to promote industrialization in the manufacturing sector including provisions such as a reduction in taxable income and a grant to manufacturing enterprises that are 100 percent foreign owned provided that they are sufficiently export orientated. In 2003, the Malaysian government announced that the temporary policy allowing 100 percent foreign ownership in manufacturing would continue indefinitely. To this end, a number of sub-sectors were identified as “strategic” and given favorable treatment, including tax holidays, income tax exemption, investment tax allowance in the form of accelerated capital allowance relative to depreciation, special deductions from income (e.g., double deduction for expenses), and other such benefits (e.g., export allowances). These sub-sectors included electrical and electronic, chemical, textile and apparel, transport, machinery and equipment, and agro-based and food products.

Carter (1992:149), citing the Australian case, raises the problem that governments are poor at identifying successful businesses or industries in which industry policy should be implemented. He suggests that the past protectionist policies have been a disaster for Australia’s economy and that there is a need for institutional and regulatory reforms in order to have less costly and inappropriate infrastructure in various sectors. To the contrary, Forsyth (1985:79-80) referring to the same case, points out that the Australian government in the 1960s through the 1980’s announced industry policies which were actually not implemented in the same manner as they were announced. Thus, problems have been created by policy ambiguity. Forsyth (1985) also suggests that a country’s overall

economic performance may improve, if decision-makers know better the direction of the economy and consistently pursue a policy of either protectionism or relying on free trade.

In 1992-93 Australia’s unemployment rate averaged over 10 percent and the duration of unemployment averaged over 12 months (Jose and Burgess 2005:2). Addressing unemployment became a priority of the then Labor government. The *Working Nation* policy document formulated an industry policy in response to the country’s economic recession and the consequential increase in unemployment. *Working Nation* declared: “As we move into the 21<sup>st</sup> century, Australian industry policy has two overriding objectives: building a competitive environment and based on this environment, building competitive firms” (Keating 1994:52). The policy program incorporated: (1) making the unemployed “job ready”; (2) paying attention to long-term unemployed and encouraging a shift from social benefits to employment; (3) reforming the public sector job placement system; and (4) introducing the principle of mutual obligation and reciprocity for the unemployed (Jose & Burgess 2005:8). In terms of expenditures, the main recommendations were: (1) the Job Compact for the long-term unemployed; (2) a subsidized training wage for the unemployed; (3) increased provision of training and work experience programs for the unemployed; (4) an expansion in pre-vocational training places; (5) increased employer payments for apprenticeship training; (6) the provision of a youth training allowance, and (7) the introduction of intensive case management arrangements for the unemployed (Jose and Burgess 2005:10). The following Coalition government dismantled Labor’s *Working Nation* in its first budget in August 1996. “However, governments, regardless of ideology, will resort to industry policy to

foster economic development and to short up election support in key electorates; liberalist values ensure that such policy will have a detached, fragmented and pragmatic character. Industry policy is thus like ‘original sin’ in a formally Christian society – everybody practices it, but you can’t get any respectable person to admit to it” (Jones 2005:36).

By comparing South Korea with a successful industry policy and the resulting rising terms of trade to Chile with no industry policy and declining terms of trade important lessons can be learned. Chile received US aid assistance that was as openhanded as that provided to South Korea, but it was much less effective (Chang & Grabel 2004:42). The state instituted industry policy in South Korea has been influential in promoting economic growth. The industrial policy focusing on R&D promotion was instituted in 1983 contributed to the development of technology-intensive information industries in South Korea. An industry policy based on financial and taxation benefits and the establishment of a national R&D consortium by government transformed the South Korean semiconductor industry from an imitator to an innovator by facilitating technological catch-up; the national R&D industry policy also contributed to the establishment of the South Korean mobile handset industry as a technological leader (Ahn & Mah 2007). State intervention in South Korea, especially in the form of industry policy, has not greatly been reduced albeit to increases in the absolute volume for world trade, international capital flows and multinational production (Kim 2003:340). However, many of the assistance measures implemented by the South Korean government during its economic development period cannot be used by developing countries nowadays; the World Trade Organization (WTO) stipulations regulate and even make illegal most

government provisions or incentives to promote specific industries (Mah 2007:77). Nevertheless, Chang and Grabel (2004:69) argue that there is some room left open for some types of protection under present WTO rules.

During the period around 1974-90 a neoliberal experiment was forced upon the Chilean economy and society. Until the early 1970s, Chile had a tightly regulated economy and financial system, with few links to international markets. The Pinochet regime deregulated the economy as part of a radical monetarist economic experiment. Although Pinochet and the junta members were not free-marketers, they decided to support the experiments by radical monetarists. The monetarist strategy was consistent with their political strategy of atomizing Chilean society to eliminate the alleged communist threat. Even though the monetarist economic policy did not have any ideological foundation, nevertheless it was perceived as politically effective (Lukauskas and Minushkin, 2000, p.716).

As a result of the radical monetarist policies in Chile, the manufacturing sector significantly shrunk its most sophisticated base and relied mostly on traditional manufacturing with slow growth. The Chilean manufacturing industry appears to strongly favor light, unsophisticated industry at the expense of heavy, sophisticated industry. Export expansion in manufacturing was a small proportion of exports. In terms of GDP there was a clear deindustrialization trend. This was in contradiction to the goal to develop industrially via exports, following the successes of the South-East Asian economies, especially Korea. Korea has developed, as already mentioned, a high-technology manufacturing industry that successfully competes internationally. While South Korea is considered a developed economy, the Chilean economy did not encourage the type

of exports that may sustain a dynamic industrial development that is based on international markets. In contrast to South-East Asia's selective interventions, a neutral and unsupervised policy that relied only on the automatic mechanism of the market in Chile was unable to shift the economy speedily and/or smoothly enough to an endogenously sustainable development path (Albala-Bertrand 1999).

This raises the issue of the Predisch-Singer Hypothesis. Prebisch (1950,1959,1964) and Singer (1950) developed the Predisch-Singer Hypothesis, by disputing the predictable wisdom of the time of free trade, as the terms of trade were contradicting the path claimed by neoclassical theory. They recommended to the newly independent states, the ex-colonies at the time, to follow a path of import-substitution industrialization. Myrdal (1956) was also a supporter of import-substitution industrialization. Even though, the Prebisch-Singer-Myrdal proposal of autarkic economic nationalist development was controversial, the national governments of the newly independent ex-colonies and many Latin American countries followed the import-substitution industrialization model.

Under the import-substitution strategy these countries required increased imports of machines and technology to achieve rapid industrialization by investing the newly acquired resources to import-competing activities. This situation demanded increased export drive to pay for imports. However, the increased imports required increase in foreign exchange that, in most cases, surpassed the growth in export earnings. These countries began to face acute balance of payments problems. As a result, to finance the balance of payments deficits, these countries became dependent on mature developed economies and international financial institutions for funding in hard currency.

## **Industry Policy and Globalization**

Given the disappointing performance of a large number of state-owned enterprises (SOEs) in the late-1980s, combined with the deteriorating economic situation and heavy debt burden faced by a number of developing countries, most developing countries underwent major policy reforms (UNIDO 1995:5). The distressed developing countries under the pressure of conditionality were advised to open up their economy to foreign trade and investment along with many structural adjustments. These reforms, which were mostly integrated into structural adjustment programs financed by international financial institutions, have taken the form of a major shift to greater market orientation and recognition of the private sector as the principal engine of industrial growth. The essential elements of this new policy approach, which is based on the Washington Consensus, have been: fiscal discipline, public expenditure priorities, tax reform, financial liberalization, exchange rate policy, trade liberalization, foreign direct investment policy, privatization, deregulation, and property rights policy in accordance to the free market approach. Industry policy has no place in the Washington Consensus and its new global economic order. However, this does not have to be the case in this globalized world.

FDI can play a key role in improving the host country's capacity to respond to opportunities offered by global economic integration, a goal increasingly recognized as one of the key aim of any development strategy. However, externalities from FDI are not produced automatically; hence an industry policy is imperative that targets and positions FDI to ensure wider externalities (Bailey et.al. 2007:454).

The globalization concept implies that a growing share of FDI is worldwide in scope and developing and transition countries, in

particular, should be able to attract an increasing percentage of FDI. Globalization, in terms of opening borders (not in terms of immigration), abolishing currency restrictions, liberalizing trade and prices, and advances in technological, transportation and communication, facilitates decisions for FDI and creates opportunities for efficient, less risky, and less costly FDI projects, especially in developing and transition economies. The UNCTAD (1996) report pointed out that the globalization process is reducing the importance of traditional FDI determining factors, replaced by non-traditional factors (Zanatta and Queiroz 2007:421).

Meanwhile, FDI inflows and outflows by MNEs and the consequent direct and indirect effects of FDI on the host countries' economies may be viewed as a vehicle of globalization. Many countries opened up their economies to trade to receive FDI inflows. However, the share of FDI is not the same in all countries and the FDI inflows in less-developing or poor countries show little or no growth (Bitzenis 2003,2004,2005). The limited extent of liberalization reforms, ineffective transition programs, unsuccessful institutional and structural reforms, unsuccessful privatization programs, and the limited enterprise restructuring process all reaffirm the need for the presence of an industry policy in this globalized world.

However, FDI experienced a crash in 2001-04. A variety factors are responsible for the dramatic decrease in FDI flows. First there was a slowdown in the world economy which reduced world demand and accelerated the global restructuring process of major MNEs in sectors characterized by excess capacity. Especially in 2001 and afterwards, the decline was due to the terrorist event of 11 September 2001 in New York City. The decline in 2001 which was mainly concentrated in developed countries was also a result of a decisive drop in cross-border

mergers and acquisitions. The economic recession especially in the USA and the EU (15) intensified competitive pressures, and thus forced companies to search for cheaper locations, explaining the stable FDI flows to the CEE region. However, on account of a strong increase in FDI flows to developing countries, 2004 saw a slight rebound in global FDI after three years of declining flows.

MNEs are the main vehicle of trade and FDI and, therefore, facilitate world economic integration and thus globalization. The increasingly highly competitive worldwide investment environment, which offers various opportunities for MNEs, together with the changing opportunities a country has to offer over time, and the different ways in which MNEs evaluate those opportunities, supports the changing character of industry policy in this globalized system. Nowadays, industry policy must include features that offer new investment opportunities in the context of globalization in order to attract FDI flows and to integrate the market economies of developing and transition economies. MNEs, FDI, trade, integration and globalization offer opportunities for a new type of industry policy especially for developing and transition economies. However, currently FDI policy, especially for R&D activities, cannot only be restricted to fiscal incentives and grants. To be able to attract and promote FDI in R&D activities diverse measures are required to create an adequate national environment, incorporating institutions, infrastructure, the economy and education (Zanatta & Queiroz 2007:420). The globalization of R&D has become increasingly concentrated to take advantage of economies of scale and clusters of knowledge but at the same time happen to be increasingly dispersed in order to access well-educated and likely low cost employees and diffusing innovations into global markets (Huggins et al 2007:447).



China and India have been implementing more articulated and consistent policies, in contrast to Brazil, consequently attracting FDI in R&D activities (Zanatta & Queiroz 2007:419). In the case of the Irish “miracle,” while the model is based on wage restraint it does not fit neatly in the neoliberal conception of international development (Bailey et al 2007:459). The Irish shifted policy away from just attracting FDI to a more sophisticated industrial policy that was characterized by (1) the provision of “aftercare” to upgrade foreign plants and to situate foreign plants within the wider economy by improving linkages, and (2) fostering domestic entrepreneurship (Bailey et al 2007:465).

The transition process also had to incorporate an industry policy. The transition economies presented an opportunity to multinationals to expand into new markets and extend their productive base. The transition process involved stabilization, liberalization of the domestic and external economy, structural and institutional reform, privatization and restructuring of the state-owned enterprises, the creation of a sound business environment in order for private companies to be established, with the ultimate aim of developing strategic comparative advantage and integrating these economies through international trade and investment. But integration required a re-orientation of trade, an increase in FDI, privatization, successful institutional reforms, and a new industry policy in order for the economy to increase its competitiveness and to survive in the global and integrated economic system (Bitzenis & Marangos 2007).

During transition, governments preferred to attract foreign investment projects in specific economic sectors. Thus, there was specific industry growth based on privatization of SOEs and through an increase in the private sector with the creation of new

enterprises based on significant incentives offered in order to improve and facilitate entrepreneurship and private ownership. Thus, most of the Central and Eastern European economies, and especially the South East European economies, have targeted the service sector and changed their initial levels of industrial production that they had in 1989. For example, Albania reached only 28 percent of its level of industrial production in 2003 compared to the level the country had in 1989, and its GDP level in 2003 was 123 percent of its level in 1989 (Bitzenis 2006). This was the result of a new industry policy focused on Albania’s service sector. In sum, as the experience of industry policy demonstrates “there is no single template for selective industrial policy across developing countries” (Chang & Grabel 2004:77).

### **Conclusion.**

Laffont (1996:1) defined industry policy as the major task of economics and political science, which is to explain the pattern of government intervention in industries. Industry policy refers to government actions to develop and/or support various industries in order to maintain the global competitiveness of their economies and industries. Industry policy can exploit country-specific advantages, such as tourism. It can also offset problems associated with the unequal income distribution among regions within the economy. For example the establishment of firms in Western Thrace of Greece has the goal to increase entrepreneurial activity in the local economy to reduce the high unemployment. However, the needs of the nation and government preferences vary over time, so the government may alter industry policy to boost exports, increase competitiveness, secure local employment, protect local enterprises and their products, or to stimulate economic

growth. Thus, industry policy may vary among countries due to differences between developed and developing countries, given the different economic conditions. Most importantly, in the era of globalization, industry policy does not become obsolete. Rather, it requires a new type of industry policy incorporating the new globalized economic conditions.

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## Interlocking Directorships

*Bruce Cronin*

### **Introduction**

When a director of one company at the same time serves on the board of another company, the two companies are said to be interlocked by that director. Through this linkage each company has potential access to information about the activities of the other, either explicitly as intelligence transferred by the director or implicitly in shaping the director's perspective and general views. Director interlocks formed by executive directors, employed by the firm, are generally interpreted as more instrumental for the firm than those formed by non-executive directors. Firms often interlock with two or more firms and those firms, in turn, with others; as a web of social relationships envelops business.

### **History**

The first studies of interlocking directorships were undertaken by the US government in the early 1900s during investigations into collusion in the railroad and banking industries. The Pujo Commission mapped the director interlocks among the principal US banks and finance companies as part of their identification of a 'Money Trust' around J. P. Morgan & Co. (Pujo Commission 1913). The interlocks were widely interpreted as a mechanism by which the companies operated a cartel, setting prices and regulating markets among the members of the trust (eg. Brandeis 1967) and on a populist wave the 1914 Clayton Act outlawed director interlocks among competing firms.

Directors themselves tend to be dismissive of the potential for interlocks to provide coordinating or collusive benefits for firms, seeing directors generally having little influence over the operational level at which price setting and other market activities take

place. The phenomena of interlinks is not seen as evidence of collusion but merely reflecting the limited supply of skilled and experienced candidates. However, utilising methodological advances in the field of social network analysis, the study of interlocking directorships has become increasingly sophisticated, allowing the identification of persistent patterns of interaction that go beyond supply shortages or mere chance.

Further, instances of large scale collusive and fraudulent behaviour among leading US and UK corporates in the late 1980s and most recently in 2002 have led to a renewed review of the independence of external directors by capital market regulators, drawing on some of this research. In 2003 the New York Stock Exchange amended its listing rules to require that a majority of board members have no 'material relationship' beyond share ownership in the company, including having served as an employee of a commercial partner or advisor during the previous three years (NYSE 2003:4).

### **Models of Corporate Governance**

Concern about the collusive potential of director interlocks resides primarily in the US and UK, where the board of directors is seen as an important counterbalance to the personal interests of managers. In these countries, directors, elected by a firm's shareholders to represent their interests, establish broad parameters for the day to day activities of the firm's management, in an effort to minimise opportunist behaviour by the latter for personal gain. The ability of directors to scrutinise managerial activity has thus been increasingly seen as critical in the light of poor performance and instances of fraud and the degree of participation of executive directors in board activities has come into question. While there has been a growing emphasis on the importance of non-executive or 'outside' directors in ensuring

oversight independent of management, such scrutiny is seen to be compromised when directors hold a material interest in the firm, such as that provided by interlocks with interested parties.

In the UK there is little statutory prescription regarding the governance structure of firms, beyond the requirement for any firm to have two directors and to report to shareholders annually on their stewardship. But the general form of governance of firms listed on the UK Stock Exchange is the representation of shareholders by a board of 8-10 directors, chaired by a non-executive director but including the chief executive and 3-4 other executive directors. Senior managers additionally normally meet separately and more frequently as an executive committee. Since the Cadbury Report (1992) on corporate governance there has been increased emphasis on the role of non-executive directors on boards and more explicitly defined governance tasks (Conyon 1994).

United States legislation is more prescriptive, with the Securities and Exchange Commission regulating the listing rules of stock exchanges and enforcing corporate disclosure about governance arrangements. The boards of the largest US firms tend to have 9-15 members. As with the UK, boards combine inside and external directors but in the US executive directors are a minority, typically 30%, reflecting the more prescriptive regulation of governance arrangements. Only around half of these external directors could be classified as independent, however. Further, unlike the UK, boards are normally chaired by the chief executive or a former executive (Coles & Hesterly 2000).

The counterpoising of shareholders and managers is less stark in the governance structures of Continental Europe where a

range of stakeholders is normally represented on corporate supervisory boards and executives are statutorily excluded. In particular, reflecting the importance of institutional capital funding, banks and large institutional shareholders are typically directly represented on German and French boards. French chief executives are widely represented on many other firms, something as a duty to the general managerial corps. Large firms in both countries have statutory representation from the workforce on the supervisory board. Thus, by integrating a range of stakeholder perspectives into the governance structure in Continental Europe the issue of director independence from management tends to be of less concern; the emphasis is on an institutional 'balance' between managerial and supervisory boards (McCarthy & Puffer 2002).

A similar concern to balance stakeholder interests characterises the Japanese model of corporate governance. Not just banks, but a web of businesses with mutual interrelationships, are represented in the governing consultations of *keiretsu* business groups. Further, government agencies are also represented through the *amakudari* system where retired officials are employed in private sector managerial positions. Consequently Japanese boards have been typically large, with an average size of 30, and independent outside directors are rare. While *keiretsu* ties weakened with the crisis of the Japanese banking system and growing foreign acquisitions through the 1990s, changes to the governance system towards the US model, such as the 2002 Commercial Code, were largely cosmetic, power remaining with the personal network around the corporate president (Ahmadjian 2000).

### **Structures of Capitalisms**

These national differences in governance structure are reflected in the considerable

body of research from the 1970s that has identified distinct structures of director interlocking in different countries. Together, these differences support the notion of distinctive 'national capitalisms'.

In a systematic cross-national comparison of the concentration of director interlocks Stockman, Ziegler and Scott (1985) found the number of interlocks per firm lowest in the UK (4.7), higher in the US (10.46), and highest in continental Europe (12.36). Windlof (2002) found a more pronounced pattern in multiple interlocks with another firm, lowest in the US (0.6%) and UK (2.1%) and much higher in continental Europe (14-23%). Recent investigation into cross-national directorate interlocks has found only minor variations on this pattern, with the identification of discrete 'Atlantic', European and Japanese networks (Carroll & Fennema 2002).

Scott (1991) argues that the distinct Anglo-American interlock structure reflects the greater reliance on financial institutions for capital funding in these countries. By contrast, the greater concentration of interlocks in Europe reflects the closer institutional arrangements between banks or investment companies and industry there. Similarly the directorate structure of Japanese *keiretsu* or South Korean *chaebol* can be related to their distinctive capital funding structures. However, restricting director relationships to a matter of capital funding is somewhat reductionist. In fact, studies of the interlock structure in the Anglo-American semi-periphery (Canada and Australasia) have found much greater interlock concentration there despite similar capital market structures to the US and UK (Ornstein, 1989; Alexander, 1994).

Moreover, at a firm level, in the US at least, little evidence of a relationship between capital dependence and interlocks with financial firms has been found (Mizruchi &

Stearns, 1988). Rather, director interlocks vary with other firm characteristics, interlocking greatest in larger firms, financial institutions, firms with major minority shareholders, and domestic rather than foreign firms (Dooley, 1969; Ornstein, 1984; Carroll & Armstrong, 1999).

In general, studies of director networks have identified a unitary structure within a country, with secondary cliques around regions (in the US) or financial institutions (Dooley 1969; Sonquist & Koenig 1975; Mariolis 1975; Mintz & Schwartz 1981; Mizruchi 1982).

### **What do Interlocks Do?**

The populist legacy of antipathy to cartels informed initial attempts to analyse the managerial implications of director interlocking, interpreting these relationships as mechanisms of collusion to various degrees. Mace (1971) pointed to the potential regulatory transgressions arising from the flow of inside information from board to board, while directors themselves insisted they erected Chinese walls against any conflict of interest. Early research focused on the influence of major family-owned corporate groupings, such as Morgan and Rockefeller (Domhoff 1967; Zeitlin 1974), including ties and interchanges with government personnel (Freitag 1975). These institutional overlaps were seen to provide the basis of the shared ideological outlook and cohesive action of a capitalist social class. Yet for every case of business cohesion, there has been little shortage of cases of business division and disunity (See Mizruchi's 1992 survey).

Less instrumental variations of interlock research have concentrated on resource advantages accompanying interlocking. Indirect interlocking with competitors has been found to increase in times of industry uncertainty, for example (Lang & Lockhart

1990). Financial institutions, in particular, have been seen to constitute significant intersections within the interlock networks. These would recruit directors from major companies to their boards to assist their general business intelligence (Baum & Stiles 1965; Mintz & Schwartz 1981). Some studies suggest a tighter relationship, finding that banks tend to draw their directors from the companies they lend to (Bearden 1987) or arguing that banks place representatives on the boards of companies they lend to as a means of closely supervising their investments (Sweezy 1953; Kotz 1978). Some, following Hilferding's suggestion, argue that concentrated director interlocks between banks and industrial capitalists represent a distinct form of business, finance capital (Fennema & Schijf 1979; Overbeek 1990; Carroll 1986). On balance, however, such finance-centred networks appear to be fluid, representing a 'polyarchic' rather than 'oligarchic' financial hegemony (Mintz & Schwartz 1985; Scott 1985). Direct resource-exchange activities seem able to account for at best a small minority of directorate interlocks.

Less conspiratorial accounts are now more prominent, with interlocks seen to provide directors with a 'scan' of the business environment and business practices. The process is evident in the following accounts by non-executive directors reported by McNulty and Pettigrew (1999:54, 63):

[Name of country] I knew well ... it has enormous potential. I said "go there, acquire a good team of people and you will get in at a price which is sensible and attractive". That they have done.

[On joining the firm] one of the first things I said was "what about strategy and plans". At [name of another company] we have ten-year, three-year and one-year plans ... they do not have that ... So next week at [name of

company] we are going away for two days to a hotel down in the country and we are having senior executives put out as close to their first shot of a plan.

The scan, the breadth of current experience, is a major reason in the appointment of external directors (Useem, 1984). Information gained through this scan is given priority by directors because the sources are familiar, a major factor in social learning (Bandura 1986; Galaskiewicz & Wasserman 1989). The direct contact also allows intimate knowledge (Davis, 1991; Meyer, 1994). Directors who have been parties to the adoption of a practice in one firm may become committed advocates of this in other firms (Palmer *et al.* 1993). However, direct contact is not always necessary; structurally equivalent networks are likely to expose participants to similar problems and solutions (Burt 1980).

On one level, the business scan is seen by some as providing the basis for an important governance function for the economy as a whole. Directors at the centre of this broad information network are seen to form a core 'inner circle' with privileged influence on decisions on economy-wide capital allocation and regulation (Mintz & Schwartz 1985; Useem 1984). While this brings us back to the realm of elite collusion, to some extent, detailed investigations into the 'inner core' have found a much more dynamic process of alliance, defection and social learning, underpinning increased board activism, for example (Westpahl & Zajac 1997). Thus, examination of the role of the business scan made possible by director interlocks has concentrated increasingly on the individual firm level.

Yet evidence of a systematic relationship between director interlocks and profitability has been elusive (Fligstein & Brantley 1992), suggesting that the potential information channels identified are used in only a limited



manner. In part, this finding may reflect methodological limitations; research in this area is almost universally cross-sectional, while social learning is a longitudinal process. For example, director interlocking has been found to be a frequent *response* of firms to financial difficulty (Richardson 1987; Mizruchi & Stearns 1998), so a simple cross-sectional association between interlocks and profitability is unlikely to be found. Similarly, the *content* of information passed through interlocks may change over time (Westphal *et al.*, 1997). And the *context* of the information may change, as when alternative information sources are available such as business media coverage of an organisational practice (Haunschild & Beckman 1998). Few studies examine the specific mechanics of the transfer of information through interlocks (Mizruchi, 1996).

Comprehensive investigation of network effects is also hindered by the wide variety of interlocking that takes place among directors. Interlocks arise in many ways and do not necessarily simply constitute an instrument for the firms involved (Ornstein 1984). Some interlocks may be intentional, aimed to secure specific relationships with other firms, resource-associated 'strong ties'. In other cases, the intentionality may be less clear, as when a 'professional' director is recruited because of their broad links with the general business community, scanning-associated 'weak ties'. Other links may arise accidentally, when a director is selected for their experience or acumen.

Longitudinal studies of director interlocks between pairs of firms broken by retirement or death have found only around 15% subsequently replaced, undermining suggestions of collusive or resource dependent behaviour in this activity (Koenig *et al* 1979; Palmer 1983; Stearns & Mizruchi 1986), although there is some association

with profitability among such ties (Richardson 1987). However, around half of broken ties are reconstituted with similar *types* of firms, which, while unassociated with profitability, does support the notion of interlocks providing channels of broad business intelligence.

Despite the conceptual challenges of identifying the mechanisms of these inter-firm relationships and their embryonic status, there is growing evidence of the effect of these intelligence channels on the strategies and governance of major firms. A variety of studies have now found the adoption of a range of business practices associated with director interlocking.

Geletkanycz and Hambrick (1997) identified a relationship between director interlocking and a firm's conformity with the typical strategy in an industry in terms of resource allocation such as capital, advertising, research and development and overhead spending and gearing. The greater the number of directors from outside a firm's industry, the more divergent the firm's strategy from the rest of the industry in these terms. Westphal *et al.* (2001) also found an indirect effect in these terms. The more interlocked firms conformed with the resource allocation norms of an industry, the more the focal firm did as well.

Haunschild (1993) found managers imitated the corporate acquisition behaviour of firms they served on the boards, particularly if these were firms in similar industries or banks (Haunschild & Beckman 1994). Further, premiums paid for acquisitions were similar among firms sharing directors as well as among those using the same investment banker (Haunschild 1994). Again, Westphal *et al.* (2001) found a secondary effect of director interlocks on acquisitions. The more interlocked firms imitated the normal

acquisition pattern in an industry, the more the focal firm did as well.

Separate studies have identified the spread of a number of tactical defences to the wave of hostile takeover attempts in the 1980s via the interlocking directorate in the United States. Davis (1991) examined diffusion of the poison-pill defence, where managers issue an option for shareholders to purchase shares at a great discount in the event of a takeover without board approval, thus greatly increasing the cost of the takeover. Firms sharing directors with firms that had adopted the tactic were more likely to adopt it themselves. Wade *et al.* (1990) found the incidence of golden parachutes, where managers receive large compensation payments in the event of a takeover and thus increasing the vigour of defence, positively associated with the number of boards a CEO served on. In Davis' (1991) study, however, where interlocking directors had a material interest in the firm, and thus were damaged by the reduction in shareholder value, a constraining effect was evident. Similarly, greenmail, a firm repurchasing its own stock at an above-market price, was found less likely where director interlocks involved a material benefit for the director (Kosnik, 1987). So, different tactics appear to be diffused through different interests in director networks.

The diffusion of business practices through director networks extends to the very organisational structure of firms themselves. Alongside economic influences, firms sharing directors with firms using a multidivisional structure have been found more likely to adopt the same form themselves (Palmer *et al.* 1993; Fligstein 1985). Similarly, Mizruchi & Stearns (1994) found large US firms borrowing a greater proportion of funds when sharing directors with financial institutions. They speculated this may reflect greater access of these firms to information or advice

on funding or greater confidence by lenders in firms they have greater knowledge of.

More specific business practices also appear to diffuse through director networks. Chua and Petty (1999) found Australian firms more likely to adopt ISO quality accreditation if they shared directors with firms that already had this accreditation. While Westphal and Zajack (1997) found that firms did not directly imitate the compensation policies of interlocked firms, O'Reilly *et al.* (1988) found CEO salaries strongly associated with the average salaries of the external directors on the compensation committee and Westphal *et al.* (2001) found an indirect effect. The more interlocked firms conformed with the compensation norms of an industry, so too did the focal firm.

The activities of business in society are also influenced by director interlocks, at least in the US. Galaskiewicz & Wasserman, (1989) found the pattern of corporate charitable donations associated with the donations of interlocked firms. Mizruchi (1992) found corporate contributions to political campaigns more strongly associated with director interlocks, particularly with financial institutions, than particular interests of firms. Burris (1991) found executives with multiple directorships more likely to donate to Republican candidates but firms with more director interlocks more likely to contribute to Democrats, firm contributions more influenced by defence contracts and issues of regulation (Burris 1991). More interlocked firms, particularly those at the centre of the interlocking directorate network (Mintz, 1995) also commit more resources to lobbying government.

Thus, the network of interlocking directors appears to play an important role in spreading business practices from firm to firm and generalising specific practices as industry norms. While information on these practices is readily available in the business media and

professional forums, the trusted or insider character of directors appears to add some legitimacy or perhaps privileged knowledge of their applicability.

Given the limited explicit acknowledgement of this process by board members, as shown by Useem's (1984) interviews for example, this method of diffusing business practices is unlikely to be professionally rigorous. Business practices are more likely to spread through this channel by chance, whim or bandwagon than by measured evaluation of alternatives. This suggests that the channel may represent a significant weakness in the governance function of boards of directors.

Thus, while in governance terms great store is relied on external or non-executive directors as a countervailing influence to internal managerial interests on boards, the study of interlocking directorships suggests the independence of these figures is overstated. Not only are external directors recruited from a limited social and managerial circles as the executive directors, the interlocking underpins an often homogenising community, whether in the extreme of links to an 'inner circle', or more broadly as a conduit for trends in business practice.

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## Islamic Governance

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### **Introduction**

What is governance? The online Oxford English Dictionary defines it, rather blandly, as “the action or manner of governing.” A more useful definition of governance is “the traditions and institutions by which authority in a country is exercised” (Kaufmann et al 1999:1). Islamic Governance, then, would be how “the traditions and institutions” unique to an Islamic society affect its governance. It would be useful to distinguish between “Islamic Governance” and “governance in Islamic countries.” The former is religiously ordained governance while the latter is merely whatever form of governance exists in a Muslim country. This article focuses on “Islamic Governance.”

However, it must be emphasized that, given Islam’s 1,400 year history, vast geographical spread and dizzying array of empires, states, kingdoms, varying schools of thought/jurisprudence and internal splits, to attempt to define and categorize “Islamic governance” is as difficult a task as attempting to define and categorize “Christian governance.” That having been said, some key points can be isolated without which no system of governance could be termed “Islamic.”

Islam, specifically the Qur’an, its holy book, was revealed to the Prophet Muhammad (c.570-632 CE) over the last 23 years of his life. Persecuted by the leaders of his native Mecca, many of whom were his relatives, over his religious teachings and advocacy of strict monotheism in a polytheistic society, in 622 CE Muhammad accepted the offer of a delegation from Medina to serve as their de facto chief judge and ruler. After eight years of intermittent tribal warfare with the Meccans, by 630 CE

Muhammad was the undisputed ruler of Mecca; most of the Arabian peninsula voluntarily converted to Islam and the Muslim conquest of the rest of Arabia was begun. Over the next few decades, large portions of the Byzantine Empire (Egypt, Syria, etc) and the entire Persian Empire were conquered by Muslim Arab armies and, after bloody civil wars and succession crises, Muslim imperial rule in the region was firmly established by the first great Muslim caliphate, the Umayyad dynasty (661-750). It was during the succession crises that the first major split in Islam, which created the Sunni and Shi’a, occurred.

What then is ‘Islamic governance?’ According to its advocates, “the Islamic ideal is that of a nomocracy, that is, the rule of Divine Law [i.e., *Shari’a*, since, as stated in the Qur’an] all power, including political power, belongs ultimately to God” (Nasr 2004/2002:148-149). Since humans are not capable of altering *Shari’a*, the Law is unchanging and unchangeable. At its most basic level, Islamic Governance is the Qur’anic commandment (Qur’an 3:104) to all Muslims “to do good and prevent evil” (*al-amr bi al-maruf wa al-nahy an al-munkar*).

It must be emphasized that while Muhammad did not claim divine status, and neither is it ascribed to him in the Qur’an or by Muslims, his life is held by all Muslims as the *uswah hasanah* (the beau ideal) of human behavior, and his interpretation of the Qur’an and his decisions are unquestionable. This is termed the *Sunnah* of the Prophet (i.e., his actions, including the *Hadith*, his collected sayings). Similarly, some ultra-conservative Muslims (usually termed *Salafis*, righteous ancestors) hold that the Qur’an, the *Sunnah* and, where the *Sunnah* is silent, the practices of the first three generations of Muslims, especially the *Sahaba* or Companions of the Prophet, are the sole source of guidance for



contemporary Muslim communities since the Prophet said that the first three generations of Muslims are the best ones (MSA online searchable *hadith* database: *Sahih Bukhari* vol.3, book 48, nos 819- 820).

A more progressive interpretation of Islam holds that the main sources of Islamic jurisprudence, *fiqh*, is the Qur'an and the *Sunnah*; if no clear answer is forthcoming from the first two, then *ijma* (consensus of the scholars) and *qiyas* (deduction by analogy) is resorted to to derive a legal ruling on the permissibility or impermissibility of any given policy or action. Only the first two sources are infallible while the latter two are, in theory, open to reinterpretation.

A necessary distinction should be made between *fiqh* (Islamic jurisprudence) and *Shari'a* (literally 'path', here the Divine Path or Law that all Muslims must follow). While the two terms are often used interchangeably, *fiqh* is simply the result of human attempts to interpret *Shari'a* and should not be viewed as immutable (Ramadan 2006:3). Thus what is often called *Shari'a* should be more properly referred to as *fiqh*.

There are currently five major (four Sunni and one Shi'a; named after their founders and most prominent theological scholars) schools of thought/jurisprudence (*madhab*) in Islamic *fiqh*: *Hanafi* (Abu Hanifa 699-767 CE), *Maliki* (Malik ibn Anas 715-796 CE), *Shafi* (al Shafi 767-820 CE), *Hanbali* (Ahmad ibn Hanbal 780-855 CE), and *Fiqh-e-Jaafaria* (Jaafar al Sadiq 702-765 CE; the only one of the founders to be descended from the Prophet Muhammad) for the Shi'as. The *Hanafi* school is usually viewed as the most "moderate" or "progressive" of the four Sunni schools since it allows greater weight for *ijma* and *qiyas*, while the *Hanbali* (of which Saudi Wahabism is a direct outgrowth) is the most "conservative" since it stresses the importance of the Qur'an and *Sunnah*. However, "progressive" and "conservative"

are broad generalizations that must be viewed cautiously since no school is uniformly more "progressive" or "conservative" in all areas. The Sunni schools of thought are not exclusive and there is substantial overlap among them; similarly, the main Shi'a *madhab* (*Fiqh-e-Jaafaria* or Twelver Shism) has many commonalities with the Sunni ones. There are also fringe Shi'a schools that differ radically from the Sunni ones; these groups are often persecuted by both mainstream Shi'as and Sunnis.

The rulings (*fatwa*, pl. *fatawah*) issued by the scholars of the five *madhabs* cover all aspects of Islamic life and, hence, of governance. These areas include mainly personal issues (marriage, divorce, child custody, dress codes, divorce, inheritance rights, manner of saying prayers, extra-marital sex, apostasy, etc) but also criminal law (definition of murder and its punishment, theft, blood money payable, consumption of controlled substances, etc.), financial issues (permissibility of various modes/types of financial transactions), and so on. Punishments are usually very strict (e.g., amputation of the right hand for theft; death by stoning for adultery; flogging for alcohol consumption) but, in theory, standards of evidence are usually high (e.g., two unimpeachable male eyewitnesses to the theft; four for adultery cases) and extenuating circumstances considered (e.g., the theft must not have been due to want, in which case it is an indictment of the ruler). It should be stressed again that no *fatwa* can supersede what is written in the Qur'an or contradict *Sunnah* but, in practice, there is considerable room for interpretation and maneuver.

## History and Geography of Islamic Governance.

Some Muslims argue that the idea of the Social Contract, the basis of modern constitutionalism and of much contemporary



political theory, is actually an Islamic concept, citing as authority Muhammad's setting down in writing the terms under which he would govern Medina and the city's inhabitants agreement to them, the 622 CE *Charter (or Compact) of Medina* (Rahman 1999/1983:95; see also Denli 2006:89, Nasr 1996:87). However, there was no such written "contract" after the Meccan capitulation so the historical record is not absolutely unambiguous.

After his death in 632 CE, the Prophet Muhammad was succeeded by the four 'Rightly Guided *Khalifas*' (i.e., caliph, literally successors to the Prophet). They were Abu Bakr (ruled 632-634 CE), Omar (634-644 CE), Uthman (644-656 CE; his kinsman Muawiya founded the Umayyad dynasty as the fifth *khalifa*) and Ali (656-661 CE), the nephew and son-in-law of Muhammad. Three of these first four met violent deaths, either due to personal enmity or dynastic succession struggles, often thinly disguised as matters of principle (e.g., the Muawiya-Ali civil wars were ostensibly about Ali's alleged refusal to punish Uthman's murderers). Despite the violence of the times, the era of the first four *khalifas* is viewed by Sunni Muslims as the Golden Age of Islam, the age of the 'Rightly Guided *Khalifas*' (*al-khulafa ar-rashidun*; since they were the men closest to Muhammad and so best placed to know what is Islamic) and their actions are viewed as authoritative, but not necessarily fully binding, precedents in attempting to decide what is and is not Islamically permissible (see, e.g., Nasr 1996:93). Shi'a Muslims view Ali as the rightful heir to Muhammad and so his actions and policies are a binding precedent for them.

For the majority of conservative Muslims and Islamic revivalists, the only permissible laws and institutions are ones which were enacted during the period of the Rightly Guided *Khalifas* since nothing else can be

'authentically' Muslim (Nasr 1996:60). For example, Abu Bakar was selected by a group of prominent Muslims to succeed Muhammad and, on this basis, some Muslim scholars argue that Islam is inherently democratic (e.g., Rahman 1999/1983:102). Similarly, these scholars argue that traditional Islamic Governance already postulates a social-welfare state (since the Qur'an mandates *zakat* or poor tax) and *Khalifa* Umar's declaration that "not even a dog should die of starvation" in the land of Islam (Rahman 1999/1983:94). Thus traditional Islamic Governance had already achieved by the 7<sup>th</sup> century CE what it took the West well over a thousand years longer and so no 'reform' or 'modernization' of Islam is necessary.

By 750 CE, the Islamic empire stretched from Spain to current-day Pakistan. Governance in the Golden Age of Islam had a very strongly egalitarian flavor. But the requirement of a rapidly expanding empire meant that the earlier egalitarian ethos of a quasi-tribal society without a strict leadership hierarchy and all adult males having a say in political decision making, rapidly transformed into a resurrected Persian-style bureaucracy under an imperial caliph to rule the new lands (Crone 1996:22). However, the new Abbasid dynasty caliphs/*khalifas* exercised purely temporal authority. Unlike the four Rightly Guided *Khalifas*, they did not have authority to issue religious decrees (Sonn 2006:27-28; Crone 1996:22-23); religious edicts and determining what was and was not Islamic was under the jurisdiction of the *ulema* (religious scholars) who often served as judges and jealously guarded their prerogatives from encroachment by the *khalifas*. Similarly, Rahman (1999/83:97) argues that Islam mandates the separation of the judiciary from the executive and also an independent judiciary since Umar and Ali decreed thus.

While there is no shortage of Muslim writing on government, from the earliest days to the current, the first major Islamic treatise on government was that of the Shafi scholar and high-ranking Abbasid official al-Mawardi (d.1058 CE), whose *Al-Ahkam al-Sultaniyya w'al-Wilayat al-Diniyya* (usually translated as the “Ordinances of Government”) essentially argued that the *khalifate* was a divinely ordained requirement and obedience was due to it (Lambton 2004:85-86) but defined the *khalifa*’s role as being confined to “defense, treasury and executive” (Sonn 2006:27), i.e., a very contemporary view of the role of the *khalifa* as simply the executive branch of the government. It was understood that the *khalifa* would promote, protect and preserve Islam but that was not the *raison d’etre* of the state. However, obedience to it was divinely ordained and so dissent was an act against God’s will (Lambton 2004:108).

A very different view of the role of the *khalifa* and the state was that of the Hanbali scholar, brilliant polemicist and much-persecuted reformer, ibn Taymiyyah (1263-1328 CE) whose *As-Siyasat ash-shar’iyyah* (Treatise on Juridical Politics) denounces *bida* (illegal innovation) in the *Shari’a* and for whom “The aim of the state is the triumph of the word of God and the establishment of a society devoted to the service of God” (Lambton 2004:146). Doing so is all the legitimation needed by the state or the *khalifa*; unsurprisingly, ibn Taymiyyah was the original inspiration for ibn Wahab (1703-1792 CE; the theological father of Saudi Arabia) and is the preferred theorist of most Islamic fundamentalists and revivalists who wish to return to a ‘pure’ Islam by stripping out all illegitimate innovation (*bida*) that has polluted Islamic societies and corrupted Muslim behavior. However, ibn Taymiyyah is not advocating blind obedience to the state or political passivity since it is every Muslim’s duty to actively participate in

promulgating Islam and remaining vigilant against illegal practices.

Thus, at the risk of some oversimplification, all commentators agreed that the populace owed obedience to an Islamic state. However, was an Islamic state simply one that was ruled by a Muslim, or was an Islamic state one that actively promoted the ‘true’ version of Islam and so was due obedience for that reason? There was no consensus on the issue.

### **The Challenge to Islam**

Despite severe internal schisms, power struggles, civil wars, competing *khalifates*, and the degeneracy of the concept of a universal *ummah* (a harmonious community of believers) into warring emirates and sultanates, the Islamic world did not face a potentially lethal threat to its very existence until the 18<sup>th</sup> and, especially, the 19<sup>th</sup> centuries and the encroachment of Western Imperialism onto what had been purely Muslim-ruled lands for centuries. Every other successful invader, Mongol or Turk, acknowledging the superiority of Islamic civilization, had eventually converted to Islam and been absorbed into the vast mosaic that was the Islamic world and turned into some of its most important promulgators. The Turks spread Islam into Europe as far as the gates of Vienna. However, the British in Mughal India, the French and the British in North Africa, and the Russians in Eastern Europe and Central Asia were resistant to conversion and Islam itself was in danger.

For the first time in centuries, the *Shari’a* was in need of major overhaul; practices long codified as Islamic and thus (theoretically) immutable had to change in order to meet the challenge of an invader who refused to be assimilated and absorbed into the Muslim world. However the once dynamic and innovative *Shari’a* proved to be remarkably resistant to change. The two main attempts at

Islamic Modernization, i.e., an attempt to emulate the West's industrial and financial prowess but within an Islamic framework, were those of Ottoman Turkey and Egypt in the 19<sup>th</sup> centuries; neither of them were completely successful although Turkey's was more thorough and far reaching than Egypt's.

### **Can Islamic Fiqh be 'Reformed?'**

A great deal of the debate, both within and without Islam, has focused on the extent to which Islam (i.e., the *fiqh* that forms the actual implementation of the *Shari'a*) is compatible with modernity in the sense that rules, laws and norms of behavior can be changed to bring them into conformity with the requirements of a modern, industrial society. Obviously if basic laws cannot be changed to adapt to changing circumstances governance must suffer and society is ill-served.

The extreme Orientalist view of Islam as unchanging and unchangeable was expressed by Lord Cromer, the de facto British ruler of Egypt from 1883-1907 and a leading Islamic scholar in his own right. Cromer argued that "Islam cannot be reformed... reformed Islam is Islam no longer; it is something else" (quoted in Kuran 2004a:129). While Kuran (2004a:129-130) agrees that certain passages of the Qur'an can be read as promoting fatalism and resistance to innovation, he vigorously denies that there is anything inherent within Islam that makes it resistant to change and innovation, whether scientific or social. Kuran argues that a very conservative interpretation of *Shari'a* has simply gained ascendancy within the various schools of *fiqh* and has almost completely suppressed other, more progressive, views. Thus one interpretation of Islam has been mistaken for Islam itself. However, it should be stressed that even within the dominant interpretation of *fiqh*, some jurists are more

progressive than others, although they are in a minority.

The triumph of the orthodox interpretation of Islamic *fiqh*, the view of most Sunni Muslim scholars, is exemplified by the saying that "the Gates of *Ijtihad* are closed;" that is, no further discussion, analysis or reinterpretation of the Qur'an and *fiqh* is needed or, indeed, possible. Muhammed Iqbal (2004/1934:131), an Islamic Revivalist and Modernist who was the ideological father of Pakistan, and extremely critical of European views of Islam, criticized the intellectual attitude of the traditional *ulema* that has "reduced the Law of Islam practically to a state of immobility."

*Ijtihad*, derived from the same root as *jihad* or struggle, is the process by which scholars arrive, after a thorough study of the Qur'an and *Sunnah*, at an independent decision as to whether or not an act or policy is Islamically permissible. Traditionally a *mujtahid*, one who engages in *ijtihad*, had to be an acknowledged *alim* (singular of *ulema*) of great learning and probity who had devoted his life to the study of the Qur'an, the Hadith, classical Arabic and *fiqh*. However, as the main Islamic *madhabs* formalized their teachings and the Muslim generations became further removed from the original few that would have known the Prophet personally, the consensus grew by the early 10<sup>th</sup> century CE that Muslim jurisprudence's "creative force was now spent and exhausted [and] the right of *ijtihad* was replaced by the duty of *taqlid* or "imitation"" (Coulson 1995/1964:80). That is, an extreme form of *stare decisis* (the English Common Law doctrine that legal precedents are binding and should only be overturned under exceptional circumstances) had become the norm in Islamic societies.

However, some scholars view the decision to 'close the gates' as a purely political one taken by the Abbasid *Khilafat* (750-1258 CE

in Baghdad and until 1517 CE in Cairo) as a way of stamping out political opposition to their rule and strengthening their hold on power by making the Abbasid *khalifa* the 'defender of the true faith,' the faith being defined by *ulema* such as al-Mawardi, beholden to the *khalifa* for employment, rank and prestige (see, e.g., Smock 2004; Kamali 1999). Thus the risk of an alternative religious interpretation that could threaten the Abbasid *Khalifate* politically was minimized.

It should also be emphasized that there has always existed a minority view among traditional Sunni *ulema* and other scholars that disagreed with the doctrine of the closing of the gates of *ijtihad*. Authors as diverse as, to give only more recent examples, Muhammed Abduh (Egypt, 1849-1905 CE), Syed Ahmad Khan (India, 1817-1898 CE), Musa Kazim (Ottoman Turkey, 1858-1920 CE) and many others had called for a rethinking of the 'closing of the gates of *ijtihad*' in light of the threat to the Islamic world from European Imperialism (see Kurzman 2002 for details and a more comprehensive listing and analysis of Islamic modernists). In general the traditional *ulema* bitterly opposed any rethinking of the fundamental tenets of Islamic *fiqh* and fought, often successfully, to prevent any real change from taking place. For example, Ahmad Khan was denounced as a *kafir* (unbeliever) by the *ulema* of the extremely successful and quite reactionary Deobandi school of Hanafi *fiqh* in India. This school emerged in part from the Indian *ulema's* opposition to the Islamic modernism (which included the study of English and a modern, i.e., Western, scientific education) Ahmad Khan advocated. In contrast, Musa Kazim was the Ottoman *Shaikh al Islam*, the government appointed head of all *ulema* in the Ottoman Empire (Kurzman 2002:178); however his appointment was controversial and the bulk

of the Ottoman religious hierarchy was never in favor of major reform.

Wael Hallaq, a Palestinian-Canadian (1999) and Abdulaziz Sachedina, an Indian-American (2006) are leading modern scholars advocating a new *ijma*. While their scholarly arguments have a limited audience among Muslims and non-Muslims, popular authors such as Irshad Manji, Indian-Canadian (2004), who has also called for a new *ijtihad* to reach an *ijma* more in keeping with the needs of the 21<sup>st</sup> century, has popularized this aspect of Islamic thought and practice. However, Manji's contention that all Muslims, not just *mujtahids*, have the right to practice *ijtihad* has no support among current Muslim scholars or basis in Sunni or Shi'a theological history.

However, Shi'a Islam did not adhere to the doctrine of the 'Closing of the Gates of *Ijtihad*' as they view the correct succession to Muhammad as being that of Ali (the fourth *khalifa*; the nephew and son-in-law of the Prophet) and then hereditary within the House of Ali. Therefore, no decision arrived at by *ulema* beholden to Sunni *khalifas* could be binding upon any Shi'a Muslim. Furthermore, Shi'a Islam holds that the *Imams* (leaders; here used in the Twelver Shi'a context to denote the 12 descendants of Ali that became the successive leaders of the largest Shi'a sect) are infallible in both spiritual and temporal matters, so it is the *Imam's* ruling and not the consensus of the *ulema* that determines what is and is not Islamically permissible. After the 12<sup>th</sup> Imam went into divine occultation (i.e., disappeared without a trace) in the 9<sup>th</sup> century CE, this power devolved to the *ulema* and led to the doctrine of the *vilayat-e-faqih* (guardianship of the jurists). It should be noted here that other, numerically much smaller, Shi'a sects (Ismaili, Zaydi, etc) often have radically different interpretations of Islamic doctrine and succession within the House of Ali.

Ayatollah Khomeini (1900-1989 CE), the leader of the Iranian revolution, adhered to the maximalist view of this doctrine which held that the most learned *alim*, someone who had been given the accolade of *marja e taqlid* (source of imitation; i.e., one whose decisions are correct and so capable of setting a binding precedent) had the right to adjudicate in all matters spiritual and temporal. Within the Iranian context, Khomeini as *Rahbar e Inqilab* (Leader of the Revolution, aka Supreme Leader) had the ability to unilaterally decide what is and is not Islamically permissible. His paramount authority was not acknowledged by all Shi'a high clerics, including other *marjas*, and so his ability to change accepted *fiqh* was not without theoretical limit. Practically, however, there was no effective challenge to Ayatollah Khomeini's construal of Islamic *fiqh* and he generally followed a conservative and traditional interpretation.

Given the extremely restrictive nature of mainstream interpretation, often relying on centuries old codification, whether Sunni or Shi'a, of Islamic *fiqh*, Islamic Governance, has some serious incompatibility issues with a modern industrial society. As a vocal Pakistani-British critic of a traditionalist interpretation of *Shari'a* put it:

That is why wherever the shari'ah is imposed -- out of context from the time when it was formulated and out of step with ours -- Muslim societies acquire a medieval feel. We see that in Saudi Arabia, Iran, the Sudan and Afghanistan under the Taliban. When narrow adherence to old jurisprudence becomes the norm, ossification sets in. (Sardar 2002.)

The adherents of the traditional interpretation of the *Shari'a* desire what the contemporary Iranian philosopher Abdolkarim Soroush has termed the *maximalist* approach to Islam where

"everything has to be derived from religion" (Fremont 2000). What the advocates of the new *ijma* desire is a *minimalist* view of Islam where social policies and laws are crafted in keeping with the highest ideals of Islam, e.g., the Islamic idea of sovereignty belonging to God (i.e., humans have temporary stewardship and must be accountable to God for their actions) and the true Islamic state being one that ensures liberty, justice, fraternity, democracy, and accountability of officials (Rahman 1999/1983, see Ch.16: "The Concept of State in Islam" for more details).

However, even in an ostensibly Islamic states ruled by a *khalifa* whose claim to the Sunni Khalifate was acknowledged by most Muslims, the traditional *Shari'a* was not always sacrosanct. The first attempt to systematically revise, update and actually codify Hanafi *fiqh* into a usable legal code, was the Ottoman Turkish *Mejelle* (properly the *Majallah al Ahkam e Adliya*: the Manual of Courts) of 1876; prior to this the Hanafi *fiqh* was "poorly classified and difficult to use [and] tended toward scholastic exclusivism and isolation" (Kamali 1999:150). In financial areas alone, the *Mejelle* contained at least five major departures from established *fiqh* (El Gamal 2006:30). Earlier Ottoman attempts at modernization, governance improvement and reform were explicit adaptations of French law to the Empire and often disregarded *fiqh* entirely (Coulson 1995/1964:150): e.g., the Ottoman Turkish *Penal Code of 1858* specifically excluded the *Hadd* (traditional Islamic) punishments of hand amputation for theft and the *Civil Procedure Code of 1880* allowed charging interest on commercial loans even though *riba* (commonly translated as usury or interest) is specifically banned in the Qur'an (Rahman 1999/1983:158). This triumph of Ottoman modernization and reform was not an easy accomplishment. It was the result of

almost a century of bitter struggle and virtual civil war between the traditionalists and the Ottoman reformers; a struggle spurred on by many military defeats at the hands of European armies, large-scale army mutinies, the murder of ruling sultans, and the eventual rise to power of the Young Turks reform movement.

Although the Ottoman state that crafted the *Mejelle* disappeared after World War One (the Ottoman *Khalifate* was abolished by the founder of modern Turkey, Mustafa Kemal Atatürk, 1881-1938 CE, in 1924), its *Mejelle* formed the basic law of many of the predominantly Muslim but non-confessional states (Iraq, Syria, etc) that succeeded it (Coulson 1995/1964). The *Mejelle* stands in sharp contrast to current Saudi criminal law and the current consensus of *Shari'a* scholars on the permissibility of interest in Islam. Unfortunately the *Mejelle* was an isolated and ultimately unsuccessful attempt at modernizing *fiqh* and nothing remotely comparable to it has happened in the Twentieth Century.

An additional source of controversy within Islamic Governance is the authenticity of *hadith*, i.e., how certain can Muslims be that the *hadith* are authentic? After the death of the Prophet countless "sayings" of his were recounted and there was considerable doubt as to what the Prophet had actually said. There are several collections of *sahih*, i.e., authentic, *hadiths* collected by scholars some centuries after the death of the Prophet. The most prominent of these for Sunnis, named after the scholar who collected them and verified their provenance, are the *Sahih Bukhari* (810-870 CE) and the *Sahih Muslim* (821-875 CE); for Shi'as, who distrust *hadiths* attributed to the Prophet by opponents of Ali, the most reliable collection of *hadiths* is the *usul al Kafi*, collected by al Kulaini (d. circa 940 CE). The *sahih hadiths* are, for the majority of Muslims, an integral part of the

*Sunnah* of the Prophet and thus a virtually unchallengeable source of Islamic jurisprudence, ranking second only to the Qur'an.

An elaborate science of *hadith* developed among certain *ulema* to weed out "weak" and "false" *hadith* based on their *isnad* (chain of narration) and the reliability of the original narrators. For example, the *Sahih Bukhari* contains only 2,602 (excluding duplications) *hadiths* out of apparently several hundred thousand examined by al Bukhari (see Coulson 1995/1964, esp. Ch. 5 "Concluding Stages of Growth" for more details on *hadith*). Some Muslim and Western scholars have criticized the *sahih hadith* as being fundamentally unreliable as a source of Islamic jurisprudence. However their work, e.g., that of such scholars as the Moroccan sociologist Fatima Mernissi, (1992) who amassed considerable evidence indicating that even the *sahih hadith* relating to the role of women in society are of questionable authenticity, has had no appreciable impact upon the acceptance of the *sahih hadith* as an authoritative and unchallengeable source of Islamic jurisprudence.

### **Current Islamic Governance and Practices**

Since even some of the more conservative Muslim societies, e.g., Saudi Arabia and many of the Persian Gulf emirates, have reasonably sophisticated modern economies and advanced financial systems, it should be apparent that adherence to a more traditional interpretation of *Shari'a* does not automatically relegate a society to Afghani or Sudanese levels of socio-economic development. The counter to this argument is that Afghanistan and Sudan do not have oil and many of the Gulf Emirates are awash in it; the Gulf countries can afford to hire whatever foreign technical expertise they need to run sophisticated economies fueled by oil exports.

It is also an indisputable fact that even many of the more conservative Muslim countries (excepting ones like Afghanistan and Somalia) utilize many aspects of a 'modern' legal, financial and educational system and, often, have systems of governance that owe more to their European colonial heritage than to their Islamic ones. Thus very few *ulema* raise objections to, for example, 'modern' traffic laws or corporate codes or computerized tracking systems for shipping containers in their ports. Neither do they raise objections to using telephones or fax machines instead of messages written on date palm fronds or handmade paper. Indeed, many extremely conservative Muslims argue that they are in favor of 'modernization' but against what they term as 'Westoxication.'

'Westoxication' usually involves Muslim personal and family law and the status of women, and ethnic and religious minorities in society. Thus the major objections raised by the traditional Sunni and Shi'a *ulema* are to transforming Muslim family law (i.e., over issues concerning age of consent, marriage rights, divorce laws, inheritance rights, and so on), rethinking the status of women, the allowability of an interest-based financial system and criminal law, with the most entrenched objections being raised over the first two issues.

For example, when the reformist military regime of Field Marshal Ayub Khan in Pakistan issued the mildly progressive *Family Law Ordinance* of 1961, which departed from traditional Islamic family law and instituted such changes as a husband requiring his first wife's written assent before marrying a second wife or written notice in the case of a husband divorcing his spouse, and the formal registration of all marriages, this was immediately denounced by the Sunni *ulema* as being contrary to Islam and intensified religious opposition to the regime (Ziring 1999/1997:242-243). Writing in his political

autobiography, Khan concluded that, "Any attempt at interpreting the tenets of Islam and adapting the laws to conform to the requirements of the time is a signal for the Ulema to raise the slogan of heresy (Khan 1967:106)."

The Saudi Arabian legal code, despite severe criticism from international human rights organizations, mandates amputating the right hand at the wrist for a first criminal offense (i.e., theft) and the left for a second, death by beheading for murder and drug trafficking, and so on, in addition to not allowing women to drive cars and forbidding coeducational schools and colleges. All five of the main *madhabs* (Sunni and Shi'a) view apostasy from Islam as punishable by death. While most Muslim countries do not actually have the death penalty for religious conversions away from Islam (conversion to Islam is universally encouraged), the continuing application of this ruling in conservative Muslim societies was demonstrated most recently in the case of an Afghan Muslim prosecuted for converting to Christianity. Even in a country controlled directly by the United States military, the strength of the traditional *ulema* was such that it was only after US President Bush mentioned his case on television and the US Secretary of State personally intervened on his behalf that the convert was allowed to go into exile in Italy (Wafa and Rohde 2006).

Where Islamic governments have modernized the existing system of governance to accommodate advances in economic and commercial thought since the codification of the great *madhabs*, the process has been to adapt Western laws and practices rather than rethink any essential aspect of the *Shari'a*. Kuran (2003; 2004b) details how the inability of prescribed *fiqh* to adapt to changing economic realities essentially forced Muslim traders in the Middle East, especially Egypt and Ottoman Turkey, to "demand

modern commercial courts” since “the traditional Islamic courts... did not recognize any of the new organizational forms [joint stock companies and corporations, insurance contracts, legal documents without corroborating male witnesses, etc]” (Kuran 2003:441). Coulson (1995/1964:151-153) details how Egyptian, Syrian, Turkish and Lebanese criminal and civil codes were direct adaptations from Italian and French ones.

In addition, as the Egyptian-born economist El Gamal (2006; see especially Ch. 10 “Beyond Shari’a Arbitrage”) has argued in the case of Islamic Banking, much of modern Islamic finance consists of finding the appropriate medieval Arabic terms to use to describe contemporary Western financial products/practices, making some minor changes and passing it off as “Islamic” and “*Shar’ia* compliant:” this is what he terms “the form-above-substance juristic approach to Shari’a arbitration” (2006:190).

### **Future of Islamic Governance**

As Sardar (2002) has argued, whenever Islam is perceived to be ‘in danger,’ there is a tendency among more conservative Muslims to deny that their faith, as manifested in the *Shari’a* and *fiqh*, is in any need of adapting to changed circumstances. Any change in established *fiqh* is viewed as a defeat for Islam and a victory for the West. For instance, accepting new technical innovations (airplanes instead of dhows) does not threaten the essence of Islam but allowing the Universal Declaration of Human Rights to supersede *fiqh* in determining civil and human rights relegates the *Shari’a* to the same status as any other man-made law: fallible and hence correctable. This denies the divine nature of the Koran and is a direct affront to God and so cannot be tolerated. Over the centuries the resistance to major changes or a complete rethinking of the essentials of *fiqh* has inculcated a norm of

doctrinal orthopraxy and not just of doctrinal orthodoxy. It is not enough to believe in the Prophet Muhammad and the Qur’an, one must also carry out the correct acts and make a public display of piety.

The real question for Islamic Governance is not whether, for example, Western-style life or automobile insurance is Islamically permissible but if there will be a new *ijma* for the 21<sup>st</sup> century akin to that of the 8<sup>th</sup> and 9<sup>th</sup> centuries. The current *ulema*’s consensus, after studying the great works of Islamic *fiqh* of the past millennium and more, is that conventional insurance is not Islamically permissible since it is akin to speculating on mortality and speculative transactions (*gharar*) are strictly prohibited. By refusing to consider whether or not centuries-old prohibitions against speculative transactions are even relevant in discussing contemporary insurance law, the *ulema* are ensuring that Islamic Governance is of increasing irrelevance to modern society since modern society and a traditional conceptualization of *fiqh* are incompatible without indulging in such extensive ‘*Shari’a* arbitration’ as to render the whole concept of Islamic Governance meaningless.

Thus, while major innovation and wholesale reinterpretation of Islamic *fiqh* is certainly possible, and there are progressive Islamic scholars engaged in such work, the current consensus in the Muslim world is that the gates of *ijtihad* remain closed. This is probably why most scholars engaged in an attempt to pry open the gates do so from the safety of Western universities.

### **Glossary of Common Islamic Terms**

*Alim*: pl. *ulema*. an Islamic scholar; one widely recognized as being extremely knowledgeable about Islamic law and theology.



*Fatwa*: a legal ruling concerning some aspect of Islam; usually binding only on those who accept the *alim's* authority.

*Fiqh*: Islamic jurisprudence; body of Islamic law arising out of Muslim customs and practices after the death of the Prophet Muhammad.

*Gharar*: speculation/chance; refers to economic transactions whose outcome is not known with any degree of certainty; e.g., futures options.

*Hadd*: plural *Hudud*; punishment prescribed by Islamic law and the Qur'an; generally held to be non-waivable by a judge.

*Hadith*: sayings/deeds attributed to the Prophet Muhammad; used to clarify or interpret passages in the Qur'an or to seek guidance on areas where the Qur'an is silent; one of the four basis for *fiqh*; see also *isnad*.

*Ijma*: Consensus of the believers/*ulema* as to whether or not something is Islamically permissible; one of the four basis for *fiqh*.

*Ijtihad*: the act of using one's independent judgment, after appropriate study of Qur'an and *Sunnah*, as to whether or not something is Islamically permissible; a more conservative interpretation is that only an acknowledged *mujtahid* is competent to carry out *ijtihad* about any issue of concern to the *ummah*.

*Imam*: leader; may refer to a prayer leader in a mosque; in Shi'a Islam, may refer either to the first 12 leaders of Shi'a Islam, starting with Ali ibn Abu Talib and continuing with his descendants, or to a revered Shi'a leader, e.g., Imam Khomeini.

*Isnad*: the provenance (chain of transmission) of a *hadith* used to determine if it is a reliable one; every link in the narration must be examined and the veracity of each narrator known and be beyond reproach.

*Jihad*: struggle/effort in the way of God; divided into the 'Greater *Jihad*' (the internal struggle to overcome human

frailties--greed, lust, sloth, etc) and the 'Lesser *Jihad*' (war against the enemies of Islam or against an unjust regime).

*Kafir*: unbeliever; one who denies the truth of God; *takfir* is the act of declaring a Muslim a *kafir*, previously a rare act among Muslims but becoming more common now among extremist Muslim groups.

*Khalifa*: Caliph; successor to the Prophet Muhammad as leader of the *ummah*; turned into a hereditary kingship by Muawiya's (the fifth *Khalifa*) nomination of his son, Yazid, as the sixth *Khalifa*; the title/position became extinct after the dissolution of the Ottoman *Khilafah* by Mustapha Kemal in 1924.

*Khilafah*: Caliphate; may also refer to God granting humanity trusteeship over the Earth.

*Madhab*: School of Islamic jurisprudence/thought; see main text for detail on the five great Islamic schools.

*Marja e Taqlid*: Worthy of imitation; highest Shi'a accolade awarded to an *alim*; implies that his rulings are correct and binding upon others who do not have the same level of learning/knowledge.

*Mujtahid*: one deemed capable of carrying out *ijtihad*; that is, an *alim* whose personal probity and mastery of Classical Arabic, *Shari'a*, *Hadith*, etc., is acknowledged by the *ummah*.

*Qiyas*: reasoning by analogy from established precedent; a process by which an *alim* determines whether something on which the *Qur'an* and *Hadith* are silent is Islamically permissible or not; one of the four basis for *fiqh*.

*Qur'an*: divine revelations made to the Prophet Muhammad over the last 23 years of his life; collected and compiled in its present form during the reign of the first three Khalifas (632-656 CE); one of the four basis for *fiqh*.

*Rahbar e Inqilab*: Leader of the Revolution; not an Islamic term; a title bestowed upon the Ayatollah Khomeini of Iran.

*Salafi*: literally ‘ancestors;’ Islamic purification movement designed to return Muslim practice to the original ‘pure’ Islam of the first three generations of Muslims; most reactionary and retrogressive of Muslim extremist movements, rejecting all innovation after the third generation; based upon a *hadith* that stated that the first three generations of Muslims would be the best ones.

*Sahaba*: the Companions of the Prophet Muhammad; the first generations of Muslims, the ones who knew Muhammad firsthand.

*Shi’a*: contraction of Shi’at Ali; the Party of Ali; the supporters of the Prophet Muhammad’s cousin and son-in-law’s claim to be his successor; this was the first major schism in Islam and there are now major theological differences between Shi’a and Sunni Muslims.

*Shari’a*: Divine Path; the guide to human conduct (personal, public, business, etc) laid down by God; *fiqh* is the human attempt to comprehend the *Shari’a*.

*Sunnah*: the Way of the Prophet; the sayings and actions of the Prophet Muhammad that act as a guide and binding precedent for Muslims; one of the four basis for *fiqh*.

*Sunni*: Muslims who rejected the claims of Ali’s partisans that he was the divinely ordained successor to the Prophet Muhammad; accept the legitimacy of the first three *Khalifas*; constitute the large majority of Muslims worldwide.

*Taqlid*: Imitation/following; sometimes used in the negative context of blind following but some conservative Muslims argue that *taqlid* is a positive duty on all Muslims to follow the guidance of the *ulema*.

*Ulema*: plural of *alim*;

*Ummah*: community of believers (Muslims).

*Zakat*: obligatory poor tax paid by Muslims; traditionally calculated as 1/40<sup>th</sup> (2.5%) of movable assets.

\* I wish to thank Bahar Davary and two anonymous referees for their valuable comments. The usual caveat applies.

### Selected Internet Sites

*Compendium of Muslim Texts.*

[www.usc.edu/dept/MSA/](http://www.usc.edu/dept/MSA/)

*Islam and Feminism.*

[www.crescentlife.com/thisthat/feminist%20muslims/feminist\\_muslims.htm](http://www.crescentlife.com/thisthat/feminist%20muslims/feminist_muslims.htm)

*Women in Islam.*

[www.usc.edu/dept/MSA/humanrelations/womeninislam/](http://www.usc.edu/dept/MSA/humanrelations/womeninislam/)

[www.islamfortoday.com/women.htm](http://www.islamfortoday.com/women.htm)

*Homosexuality and Islam.*

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*Islamic Science.* [www.cyberistan.org/islamic/](http://www.cyberistan.org/islamic/)

*Islamic Medicine.*

[www.iiim.org/islamed3.html](http://www.iiim.org/islamed3.html)

See also [en.wikipedia.org](http://en.wikipedia.org) for a very large number of entries on Islam and the Qur’an and Islamic law, science, economics, gender relations and so on. However, some of the entries have been written by polemicists and/or are of mixed reliability.

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### **Introduction**

The economic approach to law, or “law and economics,” as it is commonly known, is most generally understood as the application of economic principles to the study of the law, including its design, execution, and enforcement. The title of “law and economics” covers a wide range of approaches, but by far the most popular is neoclassical law and economics, usually associated with the “Chicago school” of economics.

For a detailed history of neoclassical law and economics, as well as other approaches to the field, see Mercurio and Medema 2006. See also Posner 1998a for a classic but up-to-date statement; Shavell, 2004 for a recent treatment; Cooter and Ulen 2004 for a comprehensive text; and Posner and Parisi 1997, Backhaus 1999, and Bouckaert and De Geest 2000 for comprehensive reference volumes.

Neoclassical law and economics assumes that all participants in legal processes—plaintiffs and defendants, lawyers and judges, criminal and police officers—are rational utility-maximizers who respond to legal incentives as they would to market prices. Through this mechanism, legal rules, procedure, and sanctions are chosen by the appropriate authorities in order to elicit behavior leading to optimal outcomes, usually measured by an efficiency criterion such as Pareto optimality or Kaldor-Hicks efficiency. The study of how individual agents respond to legal incentives comprises the positive side of law and economics, and the determination of optimal legal rules, procedure, and sanctions make up the normative side, though the distinction can easily become blurry.

This chapter will summarize the main components of law and economics, including criticism when important. (For this point on, I will use the term “law and economics” to refer to Chicago/neoclassical law and economics unless indicated otherwise.) Section 1 will introduce the foundational concepts of law and economics: utility-maximization, the Coase Theorem and transaction costs, and the two standards of efficiency utilized in law and economics, Pareto optimality and Kaldor-Hicks efficiency. Section 2 will discuss the economic approach to the basic areas of private law: tort law, contract law, and property law. Section 3 will cover the economic approach to criminal law, and Section 4 will conclude with some general critiques.

### **Foundational Concepts**

#### *Utility Maximization*

Law and economics shares its basic model of decision-making with neoclassical economics: constrained utility-maximization, under either complete or incomplete information. (Incomplete information or uncertainty is often invoked when the probability of a legal outcome, such as a particular judgment at trial, or apprehension of a criminal by the police, is unknown.) Utility in this model is simply an index of preference-satisfaction, and preferences are defined over states of the world over which the decision-maker has some influence. (See Hargreaves Heap et al 1992, for more on the economic theory of choice.) In law and economics, and the economics of private law in particular, preferences are most often defined over monetary amounts which obtain under various circumstances. There are exceptions, such as in the economic analysis of crime when punishment takes the form of prison time, and preferences must be defined

over the amount of time spent in prison (and else monetary equivalents can be assumed).

This aspect of neoclassical law and economics has been criticized, as has the economic utility-maximization model in general. For instance, as in all utility-based choice models, law and economics ignores the existence of desire-independent reasons for action (such as Sen's 1977 concept of commitment), which often take the form of moral obligations or duties. Unlike ethically-based preference, these are not included in the preference rankings, but rather outside them. These are particularly important in law and economics due to factors such as respect for the law and moral imperatives related to the law. For instance, most persons choose not to kill, not based on a cost-benefit calculation taking into account the chance of state-imposed sanctions, but because they simply feel it is wrong and do not even consider it. Or, to take a milder example, a person may observe the speed limit when driving, not because she feels an moral obligation to maintain a certain speed—she may think the speed limit is ridiculously low—but feels the law is worth obeying for its own sake. These types of motivation cannot easily be modeled within the standard utility-maximizing framework, and suggestions regarding ways to model them have not been extensively incorporated into the law and economics toolbox (see Cooter 1998 and White 2005 for recent attempts along these lines).

Related criticisms involve the role of norms in the decision-making process; in fact, the social norms literature has spawned a self-contained, alternative approach to neoclassical law and economics. (See Ellickson 1991 and Posner 2002, for foundational work; and Mercurio & Medema 2006:ch.7, for extensive summary.) Also, the standard utility-maximization model has recently come under attack from the field of behavioral economics, and much of the brunt

of this attack has been felt in law and economics, where the cognitive and conative limitations of simple models of rational choice are seen to be particularly relevant; see Jolls et al (1998), Sunstein (2000), and Parisi/Smith (2005). (See also Posner 1998b for criticism of behavioral law and economics.)

### *Coase Theorem*

While utility-maximization is inherited from neoclassical economics in general, the Coase Theorem can be considered the foundation of law and economics as a distinct subdiscipline within economics. Derived from Ronald Coase's seminal 1960 paper, "The Problem of Social Cost", the Coase Theorem is usually stated as follows: given a clear assignment of property rights and the absence of transaction costs (costs of bargaining and negotiation), the efficient solution to a legal conflict will obtain regardless of the initial assignment of rights. The (qualified) irrelevance aspect of the Coase Theorem with regard to rights assignment (and, by implication, the role of the state in legal disputes), along with the idea of transaction costs, provides a foundation for the economic approach of private law in general, including property law, contract law, and tort law. (The literature on the Coase Theorem is vast; for representative scholarship, see Cooter 1982, Medema 1995, and Medema and Zerbe Jr. 2000.)

Simple examples such as the following suffice to demonstrate the simple logic of this powerful statement. Suppose that Alice operates a yoga studio next to Bob's record store. Alice requires a quiet environment for her clients, and Bob needs to play music to help promote his products; their interests are contradictory, and a legal conflict ensues. It would cost Alice \$200 to soundproof her studio, and it would cost Bob \$300 to reconfigure his speakers to limit the sound



reaching the yoga studio next door. Assume these are the most efficient solutions for each, although clearly the soundproofing is the most efficient solution overall.

The Coase Theorem claims that 1) if the right to control the situation is clearly vested in one party or the other, and 2) if the two parties can costlessly negotiate, then the most efficient solution will obtain regardless of the holder of the right. If Bob has the right to play his music at any volume and with any speaker configuration he chooses, then Alice will have to pay \$200 to soundproof her studio. On the other hand, if Alice has the right to limit Bob's music, then Bob will be responsible for solving the problem, and rather than pay \$300 to reconfigure his sound system, he will offer Alice a payment of between \$200 and \$300 to soundproof her studio. The assumption of costless negotiation guarantees that such an offer will be accepted, and therefore the soundproofing will be performed regardless of whether it is Alice or Bob who must pay for it. Furthermore, as long as the two assumptions are met, there is no need for lawsuits or state regulation to achieve the efficient outcome, which lends a very libertarian/classical liberal flavor to the Coase Theorem.

However, contrary to common understanding, the Coase Theorem (much less Coase himself) does not assert that the assumptions of clear rights assignments or zero transaction costs ever hold in the real world. They are preconditions for the application of the logic inherent in the theorem, which actually highlights the importance of achieving rights allocations and reducing the costs of bargaining and negotiation; the closer a legal conflict comes to the ideal conditions required by the Coase Theorem, the closer the result will be to the predictions thereof. But the conditions can never be perfectly met: while rights can be clearly assigned in many cases, transaction

costs always exist and can take many forms, such as refusal to deal in a bilateral monopoly situation, free riders and hold-outs (in collective situations), and complexity of negotiations.

This realistic understanding of the Coase Theorem also tempers the libertarian interpretation thereof, for to the extent that the preconditions do not hold, state intervention may be justified to help resolve the conflict. The easier case is if rights are clearly assigned, but negotiation and bargaining are prohibitively costly (transaction costs are high). The two parties go to court, and the judge tries to "mimic the market" (an extension of Coase usually attributed to Posner; see Posner 1998): she will attempt to determine what the parties would have found to be the most efficient solution had they been able to negotiate, and then will assign the costs to the party without the right in the situation. However, there are several problems with this "mimicry," most notably the informational problems involved with determining a solution with only second-hand knowledge of the parties' subjective costs and preferences.

More difficult, and more controversial, is the case in which rights are not clearly assigned, and it is up to the judge to determine in which party the right should be vested (so the other party can be charged with the cost of the solution). Assume that the most efficient solution has been determined by the parties, but they disagree on who should bear the costs (which itself is an instance of prohibitively high transaction costs, rendering negotiation impossible). The law and economics solution is again to mimic the market, but this time the judge must determine who would "purchase" the right, or which party values it more, if the right were vested in one party or the other who could sell it (or retain it). This solution has the same informational problems as the previous case,

but has more severe normative implications, especially for those (such as Wright 1995, drawing on the thought of Aristotle and Kant) who feel that rights are grounded in a sense of justice or fairness, not to be endowed according to an economic calculus.

### *Pareto optimality and Kaldor-Hicks efficiency*

The normative standard in law and economics that covers not only judicial decision-making in the example above, but all decisions concerning legal rules, procedures, and sanctions, is efficiency, usually in the form of either Pareto optimality or Kaldor-Hicks efficiency (also known as cost-benefit analysis). Pareto is more demanding and less controversial as an evaluative standard, but is also widely held to be less applicable. A legal or policy change is considered a Pareto improvement if at least one party is made better off by the change and no party is made worse off. In its strict form, this is also known as a unanimity requirement, since it requires universal consent (and acquires its normative justification from this), but often consent is merely inferred from estimates of monetary gains to the parties affected. (See Coleman 1980 for discussion of the normative aspect of Pareto optimality.) In any case, Pareto is widely viewed as irrelevant due to most significant policy or legal changes negatively affecting some persons, especially if allocations of scarce resources are involved.

Kaldor-Hicks efficiency solves the inapplicability problem by explicitly allowing for some parties to a change to be harmed, but this relaxation of the Pareto condition introduces more discomfort among some. A change is Kaldor-Hicks efficient if the gains to those who benefit are larger than the losses who are harmed, implying a net benefit to society. Such a change is also called a “potential Pareto improvement” (Calabresi & Bobbitt 1978) because it is possible for the

“winners” to compensate the “losers” (in financial terms) and still benefit from the change. Therefore, this (hypothetical) compensation would generate an inferred Pareto improvement if actually paid. Most law and economics scholars do not concern themselves with the lack of compensation, based on several rationales, such as the position that legislators are responsible for income redistribution, not economists, lawyers, or judges (parallel to the efficiency/equity debate in general economics, and to the first and second welfare theorems). Another argument holds that if benefits and losses are distributed evenly throughout the population over time, then the average citizen can expect net benefit over the long run from Kaldor-Hicks decision-making, which implies that such a system would be endorsed by the citizenry, an argument adapted from the social contract literature (see Posner 1983, Ch.4, and Kaplow and Shavell 2002).

But troubling aspects of Kaldor-Hicks still remain. The benefits and costs used in the calculation of net benefits are often based on willingness-to-pay, which is both hypothetical and self-reported and therefore of uncertain accuracy and reliability. Even if willingness-to-pay statements are considered trustworthy, they will necessarily be based on pre-existing resource endowments, which enables more wealthy citizens to pledge more money towards (or against) a proposed change than less wealthy ones (Coleman 1984). This problem is exacerbated by the diminishing marginal utility of income, which implies that the poor citizen’s willingness-to-pay may represent a higher (hypothetical) subjective sacrifice although of lower nominal value. Also, the Scitovsky paradox shows that any change can be found Kaldor-Hicks efficient *ex post* due to the endowment effect (Scitovsky 1941; Coleman 1980, 104-5). There is also a broader ethical problem



with Kaldor-Hicks, in that it treats one group of citizens as a means to benefit another, and insultingly so based on the mere lip-service paid to actual compensation (Kronman 1980). Pareto efficiency makes some attempt to ascertain the consent of those affected by a change; Kaldor-Hicks makes no such concessions.

## **Economic Analysis of Private Law**

### *Tort law*

The economic analysis of torts (private wrongs) is chiefly concerned with efficient precaution against accidents, achieved through the optimal choice of liability rules (Landes and Posner 1987 and Shavell 1987). If harm has occurred to one party (the plaintiff) due to the actions of another party (the defendant), under what conditions should the plaintiff be able to shift the costs to the defendant? In law and economics, the answer depends on whether cost-shifting will result to lower societal costs: the costs of precaution and the expected costs of accidents (in which the probability of an accident is affected by the level of precaution taken). In other words, the lowest-cost avoider should be held liable for the accident costs (or damages) in order to provide incentive for optimal precaution on his part, by forcing him to internalize the accident costs.

The most basic liability rules are strict liability and negligence. Under strict liability, the defendant, after being found to have caused the harm according to standard principles of legal causation, is liable for damages regardless of the level of precaution taken. Under negligence, the defendant is liable for damages only if he did not take a threshold level of precaution as determined by the court. In law and economics, this level of precaution is determined so as to minimize the total of precaution and accident costs, and is known as efficient precaution. There is legal precedent for this in the famous “Hand

formula,” described by Judge Learned Hand in *United States v. Carroll Towing Co.* (159 F.2d 169, 173): precaution should be judged sufficient if the costs of precaution were at least as large as the expected accident costs. Despite not being stated in marginal terms, this is a clear and early instance of explicitly economic thinking in tort jurisprudence, and is cited often in the law and economics literature.

Under the simplest assumptions, the standard result regarding optimal liability is that the efficient level of precaution will be taken regardless of whether strict liability or negligence holds. Under a negligence rule, the potential injurer/defendant has a clear incentive to take the efficient level of precaution since he is thereby absolved of any future liability, and also has no incentive to take more (inefficient) precaution. Under strict liability, the potential injurer is liable for any damages he may cause regardless of precaution, which implies that he will take any and all cost-justified precaution out of his own self-interest. Since he wants to minimize the precaution and expected accident costs he must incur, he will choose the efficient level of damages without court mandate.

There is, of course, much more to the issue of optimal liability rules; here I mention three prominent complications not considered above. The first concerns the trial costs under each liability rule. The informational costs are much lower under strict liability, because the court does not have to compute the efficient level of precaution, or weigh evidence regarding whether or not the defendant achieved it. Due to this informational advantage, strict liability cases are shorter, less involved, and therefore less costly than negligence cases, but there would also be more of them (since the plaintiff is always awarded damages). Given these contrasting effects, it is ultimately an empirical question which liability rule results in lower trial costs,

which would ideally be included in the total costs to be minimized by the chosen liability rule.

Second, the simple model assumes that precaution is observable and verifiable, since evidence regarding precaution must be presented at trial in a negligence case. For instance, a driver can obey the speed limit and have a blood alcohol count below the limit, both of which are observable, but she may also be tired or distracted, conditions which are not observable but may lead to an accident. In a negligence case, she may meet the standard of observable precaution and not be held liable, when actually she was negligent in a broader sense due to her impaired mental state and therefore took inefficiently low precaution. Under a strict liability rule, however, the driver will take whatever precaution is efficient regardless of observability, rendering strict liability the more efficient liability rule in circumstances in which verifiability of precaution is difficult. (The amount or level of risky activity taken by the injurer works in much the same way as unobservable precaution—under a negligence rule, the injurer has incentive to take efficient precaution only, but no incentive to choose an efficient level of activity, whereas strict liability provides incentive to optimize over both.)

Finally, precaution on the part of the plaintiff is addressed in contributory negligence cases, in which the precaution taken by the defendant is only considered once the plaintiff's precaution is assessed. If the plaintiff is found negligent, he is found liable and the defendant's precaution is never assessed, but if the plaintiff is found to have taken his level of efficient precaution, then either strict liability or negligence may apply to the defendant. Like the standard case considering only the defendant's precaution, contributory negligence also leads to efficient precaution on both sides: the plaintiff takes

his efficient level of precaution to try to shift the costs to the defendant, who then takes her efficient level of precaution for the same reasons as in the standard case.

### *Property law*

The economic analysis of property law deals with defining, assigning, and defending property rights, which is a precondition for the application of the Coase Theorem, but also an application thereof. From the Coase Theorem, we know that under ideal conditions, rights will end up with the party that valued them most. If conditions are not ideal—particularly if transaction costs are high—the court (or the state, generally) tries to reallocate property rights optimally to maximize value. Furthermore, when designing a property rights regime from scratch (in the case of new technologies, for instance), the state may use this principle to arrive at an optimal allocation from the start, another application of “mimicking the market,” and then letting the Coase Theorem operate to correct any remaining inefficiencies (assuming low transaction costs).

A clear example of this application is the rights to land. In legal terms, property rights are properly considered “bundles” of rights, specifying what the right-holder may do with various aspects of her property, including rights of transfer, disposal, use, development, etc. It seems obvious that a landowner places high value in the use of the actual land she owns, but less obvious is her interest in the ground beneath her land, or in the airspace above it. The municipality in which she lives would likely place a greater value on the ground beneath her property (after allowing space for a basement or subfloor), and if we assume that homeowners would gladly sell the rights to the ground beneath their property to the municipality, then efficiency would require vesting that right in the municipality

originally. The same principle applies to the airspace above the property, which airlines would value much more highly than homeowners, so the right is assigned to them from the beginning. (Application to intellectual property rights is very similar, and is used to justify or criticize many of the conventions and definitions of copyright and patent; see Landes and Posner 2003.)

The economics of property law also covers the enforcement of property rights—for instance, should interests in property be protected by monetary damages (in which the owner is compensated for trespass or theft) or injunctions (which prohibit trespass or theft with the threat of official sanction). These categories correspond to liability rules and property rules, as delineated in Calabresi and Melamed (1961), considered a foundational work of law and economics. Liability rules compensate the “victim” after the harm, and property rules prohibit the “injurer” from imposing the harm (with threat of sanction). Both are used to protect property in different circumstances: for instance, liability rules are commonly used in cases of property damage, while property rules are used in cases of property theft.

This division of labor among enforcement rules can be explained in terms of transaction costs. Property rules are more efficient when market transactions are relatively costless: if Jim wants Jane’s car, he can fairly easily make her an offer for it. Property rules, which carry penalties for theft, encourage reliance on voluntary market transactions when those transactions have low costs. But Jim cannot negotiate with every person whose car he may accidentally damage on a given day; the transaction costs of doing so are clearly prohibitive. Therefore, if he hits Judy’s car (by accident), a liability rule applies, and he (or his insurance agent) must pay damages (as covered in the section on tort law). Property rules are recommended when transaction

costs of *ex ante* voluntary transactions are lower than those of *ex post* legal proceedings; liability rules are recommended when the opposite obtains.

### *Contract law*

A primary topic in the economic analysis of contract law is optimal breach (Kronman and Posner 1979, Kornhauser 1986). The relevant question is: when is it efficient for one party to a contract to break the agreement unilaterally, and how can damages be set so that only efficient breaches occur? A breach of contract is considered efficient (in the Kaldor-Hicks sense) if the costs of performing the contract exceed the benefits from doing so, or, equivalently, if the costs of performance are greater than the costs of breach. If there are net benefits from breach, even if they all accrue to the breaching party, then under ideal conditions a transaction should be possible in which the breaching party can (hypothetically or actually) compensate the other party for the breach and create a Pareto improvement from a Kaldor-Hicks one via the Coase Theorem.

But of course, the party who wants to breach will do it if it is in her interest—if it is efficient for her, not necessarily overall. For this reason, remedies must be determined optimally to provide incentive for parties to breach only when it is socially efficient. The answer is motivated in a similar way to the economic analysis of tort law—the goal is to make the breaching party internalize the costs of her action, so she will only breach if the benefits to her are greater than the costs to others (which she internalizes). Such remedies are called expectation damages, representing the benefit the other party expected to gain from performance of the contract, and therefore the costs to him from the contract being broken. If the breaching party has to pay such expectation damages, then she will only breach if the benefits

exceed the costs—in other words, if it is an efficient breach. (There is another type of remedy called reliance damages, which simply compensates the other party for any expenses taken in reliance of the contract being performed, but not any benefits accruing from performance. This is obviously a lesser damage award, and will result in inefficient breaches.)

Sometimes, but rarely, a judge will demand specific performance as a contract remedy, in which no breach is allowed and the contract terms are enforced—the judge leaves any change in the contract to the parties themselves (Ulen 1984). This may seem to prohibit efficient breaches, but if the ideal conditions for the Coase Theorem obtain, the party who benefits from breach can negotiate with the other party to buy out of the contract; if the breach is efficient, and there are no barriers to a deal, then such a renegotiation will happen, and the inefficient contract will be broken. This has clear similarities to strict liability in torts: it requires little third-party calculation of costs and benefits by the court, it requires consent on the part of both parties, and leaves open the possibility of private renegotiation of remedies or damages using parties' private, subjective information.

### **Economic Analysis of Criminal Law**

The economic analysis of crime owes its classical origins to Bentham (1781) and Beccaria (1764), and its modern impetus to Becker (1968). (See also Posner 1985 and Polinsky and Shavell 2000 for important general contributions, and Ehrlich and Liu 2006 for a comprehensive collection of important literature.) Also known as the "economics of crime," this subfield of law and economics must be dealt with separately from the discussion of private law because it does not deal with disputes between private parties that admit the possibility of out-of-

court settlement based on the Coase Theorem. Instead, crime deals with state prosecution of offenders who have broken public laws that mandate punishment upon conviction. However, the motivation behind the economics of crime is similar to private law: how to structure institutions (laws, procedures and sanctions) and allocate scarce resources efficiently to minimize the overall costs of crime.

The goal of minimizing the costs of crime (inclusive of anti-crime measures, such as costs of enforcement, prosecution, punishment, etc.) implies an emphasis on deterrence of future crime as the motivation and justification for expenditures related to criminal enforcement. Deterrence, an essentially consequentialist notion, is often contrasted with retributivism, usually associated with deontological ethics, which justifies punishment by recourse to basic concepts of justice, duty, or rights (Murphy and Coleman 1990:117-24). Deterrence is often criticized by retributivists for ignoring the crime and criminal of the moment and focusing instead of the future; likewise, retributivists are criticized by deterrence advocates as being backward-looking and unconcerned with future incidence of crime and the attendant welfare effects. A third path, suggested by Hart (1968), Rawls (1971), and Byrd (1989), holds that the general practice of punishment is justified by deterrence, but specific instances of punishment must be constrained by retributivist concerns (only the guilty should—and must—be punished, punishment must be proportional to crime, etc.). The emphasis on deterrence retains the economist's expertise with scarcity and resource allocation (which retributivists have difficulties incorporating), and the retributivist aspect maintains a sense of justice, and of crimes as wrongs that must be

punished (before deterrence and broader welfare effects are considered).

Efficient deterrence, following the basic neoclassical tools of marginal analysis, requires that resources be devoted to a certain aspect of enforcement, prosecution, or punishment, until the marginal benefit of the last unit of expenditure equals its marginal (opportunity) cost; or, taking all areas together, resources must be allocated so that the marginal benefit of the last unit of expenditures devoted to each area are equal (and therefore no improvements could be made via reallocation). Marginal benefit in all of these cases refers to diminished harm from criminal activity deterred, often measured in monetary terms, while marginal cost of increased expenditure can be in monetary terms or foregone deterrent effect of alternative use of the resources (opportunity cost).

Two prime (and interrelated) examples of resource allocation with regards to deterrent punishment in the economics of crime are 1) the choice between fines and imprisonment as the form of punishment, and 2) the choice between the probability and severity of punishment. The choice between fines and punishment was introduced by Becker (1968), who concluded that fines should be used as much as possible because of their low resource cost: since fines are a simple transfer between convicted offenders and the state, the only resource cost is deadweight loss from collection. On the other hand, imprisonment involves significant real costs, including prison construction, maintenance, and staffing, as well as food, clothing, and health care for the prisoners. Assuming a given fine and a given prison term are equally deterrent, fines would be cheaper, freeing up resources to devote to other uses.

One such alternative use is increasing the probability of punishment, or, in more detail, the probabilities of apprehension,

prosecution, and conviction. If offenders, or a certain class of offenders, are particularly sensitive to the probability of punishment (relative to its severity), then devoting resources to increasing the likelihood of conviction will be of greater deterrent value and therefore will be more efficient. Of course, this involves significant social costs, so increasing probability will never be more efficient than raising fines. Hence, an early result from Becker is that the optimal punishment in simple cases is to impose high fines with minimal probability. (An example of this would be littering in the United States, where fines are often at the level of \$500 with an extremely low probability of being fined.) Becker does assume a practical upper bound on fines, due to either community disapproval of disproportionately high fines for minor offenses, or judgment-proof offenders who lack the wealth to pay high fines. So the amended recommendation becomes to set the fine to the maximum level feasible, and then set the probability to achieve optimal deterrence, in which the last dollar of expenditure on increasing probability prevents one dollar of harm from crime. (See Polinsky and Shavell 1979 for more on the choice between probability and magnitude of fines.)

Imprisonment complicates the problem, since it too has a real resource cost. (See Shavell 1985 on nonmonetary punishment in general.) But first we must deal with the question: why imprison at all? The most popular economic rationale is the infeasibility of sufficiently high fines for major crimes for reasons stated above; another reason, more retributivist in nature but still compatible with the deterrence rationale, is that monetary penalties do not seem to “fit” some particularly heinous crimes, such as murder and rape. For these reasons, economists deem imprisonment necessary although costly. But these costs, and any proposed increase in

them due to longer prison terms, must be balanced against the costs of an equally deterrent increase in the probability of imprisonment. Or, equivalently, resources must be allocated such that the marginal benefit of spending an extra dollar on prison costs (due to longer prison terms) is equal to the marginal benefit of spending an extra dollar on increasing the probability of punishment (due to more likely sentences).

But how do we know how much crime (or harm) a certain probability and severity of punishment will deter? This is based on the standard model of (expected) utility-maximization, in which the expected benefit (utility) from attempting a particular crime or a criminal “career” in general is compared to the expected cost (disutility) from being punished. For current purposes, we’ll assume that the benefits are certain; the criminal attempt will be successful. But the probability of being apprehended, prosecuted, and convicted is almost always uncertain, and this implies that the potential criminal must assess the risk of being punished, bringing in his preferences regarding risk.

Clearly, an increase in the expected cost of punishment would change the potential offender’s marginal calculation, and would predictably lead to a decision either to abstain from the crime or commit a lesser crime. This increase could take two forms: an increase in severity of punishment (higher fine or longer prison term) at a fixed probability or an increase in the probability of a punishment of fixed severity. (Obviously, both severity and probability could also increase simultaneously or sequentially.) Each would increase the expected cost of punishment, but in different ways. An increase in severity would likely impact cost somewhat linearly, absent any consideration of time discounting, in the case of imprisonment (Polinsky and Shavell 1999) or increased marginal disutility of fines, while an increase in probability is

more complicated, bringing in the offender’s attitude toward risk aversion. A more risk-averse offender would be more deterred by a more severe punishment with lower probability (assuming the expected punishment is kept the same). Such considerations are necessary to optimize punishment “schedules” (severities and probabilities) so that total criminal costs (harm plus enforcement and punishment costs) are minimized.

### **Summary and General Critiques**

As we have seen, the economic approach to the law attempts to provide a unified analysis of all aspects of the legal system using the concepts of rational choice and efficiency (including the Coase Theorem). In addition to analyzing tort, contract, property, and criminal law, the economic approach has also been applied to family law (Cohen 1987, Brinig 1990, Dnes and Rowthorn 2002), legal procedure (Posner 1973, Easterbrook 1983), and constitutional law (Posner 1987, Boudreaux and Pritchard 1993), just to mention a few topics precluded from this article by space considerations.

Any field of study as successful as law and economics is guaranteed to attract criticism, and criticism is even more forthcoming in this area due to encroachment of legal studies from economic “outsiders” (though, to be sure, many legal scholars openly welcome economic analysis). A common criticism is that while the economic approach may approximate legal outcomes, it does not capture the spirit, purpose, or normativity of the law, in general or in particular cases or areas of the law. (For instance, see Dworkin 1986 for a general criticism of the economic approach in general; Coleman 2001 for criticism of the economic analysis of tort law; and Coleman 1985 on the economics of crime.) Another point of contention is the ethical orientation of law and economics,

which is strongly consequentialist, as opposed to the inclination of some legal scholars and philosophers to adopt a more deontological basis grounded in rights and duties. For instance, there is an extensive literature criticizing the normative status of the efficiency norm in law and economics, exemplified by Dworkin (1980a,b), Kronman (1980), and Coleman (1980); White (2006) criticizes various aspects of law and economics from the viewpoint of Kantian duty-based ethics; and Geistfeld (2001) attempts to reconcile the economic approach to law with nonconsequentialist moral concerns. On the other hand, in his more recent work, Posner (1999, 2003) disputes the relevance of moral philosophy to legal studies, including the economic approach. It seems that as the application of economic analysis to the law continue to grow more comprehensive and elaborate, so do the debates over the philosophical foundations of law and economics (White 2009a), representing the ideal of extensive and intensive development of the field.

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## Legislature, Executive and Judiciary

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The distinction between the ‘three branches of government’ has long been integral to description, analysis, and evaluation of political institutions and the policy process. Conceptually, it identifies the legislature, executive and judiciary according to their respective functions in a system of representative government. Descriptively, it serves as a tool for differentiating modern democracies according to the way the branches are arranged and constituted. Normatively, it provides the basis for claims about good design of democratic institutions. And analytically, it is studied as a major independent variable in determining policy outcomes.

In general, analyses focus on the degree to which the three branches are either separated or fused; the number, electoral basis and relative powers of the legislative chambers; and the extent to which judicial systems are able to impose limitations on governments and independently influence the policy process. The now well-established principles and practices of representative democracy emerged and were refined over a prolonged period of political and intellectual struggle in a handful of leading Western countries. Recent waves of democratisation have seen these principles and practices applied and adapted in various ways and to varying degrees of success in a variety of new settings.

### **Conceptual Framework**

The distinction between the three branches of government is a venerable one that originates with Aristotle (*Politics* IV:14). Its modern use arose out of the triumph of parliament in 17<sup>th</sup> century England and the consolidation over the following century of a system of

constitutional monarchy in Britain. It was there that parliament established itself as the sovereign law-making body; the monarchy became differentiated as the locus of executive leadership and action; and the rule of law was acknowledged in the form of an independent judiciary.

Each branch is conceived as having an ideal-typical set of roles and rationales. The legislature reflects and aggregates the diverse popular will; provides a forum for discussion and debate of alternatives; and serves as a site for establishing the majority will. Thus it is ascribed the deliberative function of statutory law making. By reason of its concentrated nature, the executive branch is ascribed the dual role of leadership and initiation on the one hand and execution and implementation on the other. In its latter capacity, it is responsible for the management of the administrative apparatus of government and the operation of government organs and agencies more broadly. As a more autonomous branch, finally, the judiciary is charged with interpreting and applying the law in practice—but given its less directly accountable nature, not mandated to change the law in the process of that interpretation and application

### **Parliamentary and Presidential Forms of Government**

The difference between such an abstract conceptual tool, and a descriptive framework for concrete application is considerable. In practice, the existence, constitution, and functioning of the three branches vary greatly from country to country. It is on this basis that we define the two basic or primary models of modern representative government: the parliamentary and the presidential. Each has numerous variants, but the basic dichotomy remains clear. In addition, there has been a spate of hybrid versions combining key features of each basic model,

loosely generalised as ‘semi-presidential’ systems.

Parliamentary systems are defined as those where the executive branch is formed within and remains answerable to the legislative branch. In the British, or Westminster, tradition, this fusion of the two branches is known as ‘responsible government’. Presidential systems are defined as those where the executive branch is formed independently of the legislature and is accountable directly to the people. In the American tradition this may also be known as the ‘separation of powers’. The fusion of powers in parliamentary systems is heightened by the fact that the executive not only derives from the legislature but also dominates legislative activity—particularly in the lower house.

Parliamentary systems are characteristic of Western Europe, where they have emerged historically out of monarchical government, and have been the legacy of colonising powers to many of their overseas dominions. The presidential system was invented in the United States and was adopted by those countries within the American sphere, notably those of Latin and South America.

A major axis of difference between presidential systems is the amount and extent of power they confer on their executive branch. In the US model, the president is relatively weak, forced to compromise with the legislature on virtually every matter. The flurry of constitution making among the American colonies as they asserted their independence in the 1770s was characterised by an unmistakable predilection for subordinate executives whose role would be restricted to mere ‘administration’ — a term still very much in use today. In the South American versions, presidents have typically been granted much greater capacity for unilateral action.

## **Divided Executive**

An ancillary component of the distinction between these two basic models is that the executive in parliamentary systems is itself divided into two offices—head of government and head of state—while in presidential systems the two functions are combined. The dual structure of the parliamentary executive reflects its monarchical origins, with the executive function emerging as a joint exercise between crown and parliament. Typically, parliamentary heads of government are titled Prime Minister or Premier, and together with their ministerial colleagues they compose the ‘political executive’ known as the Cabinet or Ministry.

The head of state in a parliamentary system may be a vestigial monarch or an appointed/elected officer not infrequently called a president. The head of state has now generally been relegated to a role that is entirely or largely symbolic and ceremonial and thus may be viewed as anachronistic and redundant. Indeed, the position could—and in some instances has been—abolished altogether without affect on the operation of the system. There are cases, though, where the separate head of state retains a potential to exercise ‘reserve’ powers on matters to do with the operation of the constitution.

## **Anomalies and Mixed Systems**

Exceptions to the rule have always existed. One particularly ambiguous set of arrangements is the Swiss, where a seven-member executive council is elected in the parliamentary fashion from the legislature, but for a fixed term and thus, in the presidential fashion, is not accountable to the legislature. The position of head of government rotates annually between members of the executive council and there is no separate head of state. In 1917 Finland pioneered a hybrid arrangement that

established a direct juxtaposition of parliamentary and presidential elements as a compromise between those parties seeking a parliamentary republic and those wanting to retain characteristics of monarchical rule. In 1958 France switched to a similar arrangement. The goal was to create in the form of a significantly enhanced presidency a focal point for the nation and an office capable of strong leadership. In this semi-presidential model of the Fifth Republic, there is a directly elected head of state who exercises a number of substantive political powers (particularly those concerning military and foreign relations) as well as constitutional authority to appoint the head of government. The prime minister, however, cannot survive in office without a working majority in the National Assembly and thus must be chosen from the winning party or parties. Consequently, the system tilts towards presidentialism when the two branches are controlled by the same party and towards parliamentarism when the President is obliged to ‘cohabit’ with a hostile legislative majority. With the late twentieth century wave of democratisation, mixed systems have proliferated

Mixed systems have proven to be the model of choice for a number of newly-democratising countries—notably in Africa and eastern Europe—seeking to incorporate that unifying element and ensure strong leadership. Some of the post-Soviet regimes are overwhelmingly presidential (most notably Russia); others exhibit a more genuine balance; and some have shown signs of moving toward conventional parliamentarism in recent years, as has Finland. Responding as the French were in 1958 to the frustrations of an electoral system based on undiluted proportional representation, Israel has also made the move to a mixed system. Instead, though, of upgrading the existing head of state, Israel’s

constitutional changes of 1992 introduced the novel expedient of a directly-elected prime minister. The new system retains its parliamentary nature in the fact that the cabinet positions are filled from within the legislature and the PM can be removed by a special vote of the Knesset. The post-apartheid South African constitution similarly involves the presidentialisation of what is essentially a parliamentary system.

Perhaps the greatest analytic challenge is to squeeze the European Union into this typology. Deciding which of the existing EU institutions correspond to each of the three classical branches of government is difficult, and determining whether EU institutions tend toward the parliamentary or the presidential is even more so. A clearly recognizable judicial branch exists in the form of the Court of Justice of the European Communities (‘European Court of Justice’). A clearly recognizable legislative chamber exists in the form of the European Parliament. What might be regarded as an executive branch exists in the form of the European Commission. At this point the analysis quickly unravels, for the Commission is an appointive body and no mention has yet been made of the body that eclipses all others, the Council of Ministers. As a merely incipient federation with strongly confederal characteristics, the EU locates primary authority—both legislative and executive—in the Council of Ministers directly representing the member state governments. Should the President of the European Commission become a democratically elected position, the EU could move toward presidentialism. Should the European Parliament continue to enhance its powers, the executive would likely take a more parliamentary form. Insofar as this occurs, it is not difficult to envisage the Council of Ministers declining in status to something more like federal legislative chamber akin to the German *Bundesrat*.

## **Independent Judiciary**

Since at least the *Magna Carta* of 1215, due legal process has been regarded in Western culture as the cornerstone of a free society. The key to due legal process, in turn, has long been regarded as an independent judiciary capable of applying the law in a non-arbitrary way. In Britain, judicial independence was underpinned by the establishment of a large body of law within the judicial system itself, the common law.

How is judicial independence to be preserved? One component of such a regime is a constitutional provision making judicial action the exclusive preserve of the judicial system and prohibiting the other two branches from establishing quasi-judicial tribunals and practices. Such a constitutional rule becomes strongly self-reinforcing since the judiciary are likely to police it enthusiastically. Another component of a regime of judicial independence is the refusal to grant either the executive or the legislature alone the power to make appointments, a practice implemented in the US Constitution. When defending the draft US Constitution in 1787–88, the authors of *The Federalist*, though, placed most emphasis on lifetime appointment as the chief guarantee of independence.

## **Judicial Review**

Judicial independence does not mean a privileged status for the judiciary in the political system as a whole. While British judges administered their own judge-made law, they were in no position to question the laws passed by Parliament or to grant the common law a more fundamental status than statute law. While this was famously attempted in *Dr Bonham's case* of 1610, that was the exception that proved the rule. Judicial review in the European context was always strictly limited to considering the compatibility between administrative actions

and statute law rather than the legality of those laws themselves — legal ‘positivism’ as it is known. In Britain, this was ensured by the doctrine and reality of parliamentary supremacy or sovereignty and emphasised by such notable English constitutionalists as William Blackstone and A. V. Dicey. The subordinate role of the judiciary in the British system has always been evident in the status of the House of Lords as the highest court of the land.

By pioneering the codified constitution and making provision for an independent judiciary, the Americans established the conditions for true judicial review and effected a revolution in constitutionalism. In the landmark case *Marbury v Madison* (1803) the US Supreme Court used the fact of a codified constitution to assert for itself the role of guardian of the constitution, notwithstanding the silence of the document itself on that matter. This development finally gave concrete form to an ancient conviction that society should be governed by a hierarchy of laws that subordinate ordinary acts of government to a fundamental law of more universal validity.

Judicial review is closely associated with federalism and the need for an umpire to resolve issues of divided jurisdiction. This power is greatly enhanced where there is a set of constitutionally enshrined individual rights to enforce. Inevitably, judicial review blurs the distinction between a legislative branch that makes law and a judicial branch that merely interprets that law and in so doing raises issues about the judicialisation of politics and the democratic and constitutional propriety of so-called ‘judicial activism’. In the United States, the impact of Supreme Court decisions in such contentious areas as civil rights, religious disputes, free speech and privacy has generated an ongoing debate about the legitimate role of the courts.

Given the deep ambiguities almost

necessarily attendant upon having a written constitution, the scope for divergent or innovative interpretation may well be considerable. Whether courts adopt philosophies of interpretation that privilege a putative ‘original intent’ behind the constitution, or instead choose a legalist reading of the constitution as a text, or alternatively again seek to adapt yesterday’s document ‘progressively’ to today’s needs, will have significant impact. While famously described by Alexander Hamilton (*Federalist* 78) as the ‘least dangerous branch’, the power of review has given the judiciary a unique authority.

The British extreme is now highly unusual, reflecting the UK’s highly unusual character as one of the few remaining liberal democracies without a codified constitution. Elsewhere, the American model of a supreme court has been widely adopted — particularly in other federations such as Australia and Canada. One notable exception is federal Switzerland, where only the sub-national governments are subject to judicial review and reliance is placed instead upon the constitutional referendum. More commonly, though, continental European practice has been influenced by the Austrian innovation of a distinct constitutional court formed and operating separately from the normal legal system and not functioning in an appellate manner. The Renner–Kelsen model was developed for the 1920 Austrian constitution and is now widely practised in Europe.

In general, judicial review has gone from non-existent two centuries ago, and rare a century ago, to being widespread though not yet universal today. It remains distinctly muted in the Scandinavian democracies but has expanded greatly elsewhere. Among its attractions is the contribution it can make to the consolidation of democratic processes in the new democracies of East Asia and elsewhere (Ginsburg 2003). One of its most

prominent recent conquests has been the European Community, where the assertion of review powers in decisions of the European Court has made a significant contribution to European integration.

### **Doctrine of Separation of Powers**

The distinction between the three branches of government has played an important role in the normative science of government by providing the basis for the doctrine of the separation of powers. Originating with the radical Whigs of 18<sup>th</sup> century England; more formally expressed by the French philosopher Montesquieu; applied to varying degrees by the Americans in their intense period of constitution making from 1776 to 1788; and finally sanctified by Alexander Hamilton, John Jay and James Madison writing as ‘Publius’ in *The Federalist* papers of 1787–88, the separation of powers remains an influential set of principles for constitutional design. It provides the normative basis for the presidential system of government and its guiding principle is the principle of constitutional restraint or limited government.

From his perspective as the subject of an absolute monarch in 18<sup>th</sup> century France, Montesquieu looked admiringly at Britain’s ‘balanced constitution’ and argued that a separation of powers between the three branches of government was the way to preserve and protect individual freedoms from the potential tyranny of any one source of authority. This proved a powerful argument for the founders of the US Constitution who wished to guard against both autocratic and democratic tyrannies. The approach was pressed most notably by John Adams; first implemented in the Massachusetts Constitution of 1780; and given mature form in the US Constitution of 1787/89. In their defence of the new form of government that had emerged from the Philadelphia Convention, the ‘Federalists’

appealed repeatedly to this logic and thereby confirmed this doctrine as the underlying ethos of the presidential system.

There can be no such thing, though, as a true separation of powers; inevitably the three branches will share responsibilities. Thus there emerged in the American formulation of the doctrine a strong emphasis on the complementary role of ‘checks and balances’. This notion has two distinct components. First, the three branches would need to work in consort and consequently any one branch would be in a position to ‘check’ or obstruct the others. ‘Ambition must be made to counteract ambition’, as Madison declared in *Federalist* 51.

A consensus between the four different power centres—House of Representatives, Senate, President, Supreme Court—is necessary before government as a whole can act. Legislation must pass through both houses of Congress, be signed by the President, and not be struck down by the Supreme Court. Secondly, then, was the question whether this consensus should be easily generated or generated only with some difficulty. With difficulty, argued the Federalists: like a set of balance wheels, the three branches should run on different cycles so as to keep them out of step with one another. The houses of Congress, the Presidency, and the Supreme Court were all given different terms of office — ranging from two years in the House of Representatives to a lifetime on the Supreme Court — as a prophylactic against any burst of democratic adventurism. The US government is perpetually changing but never fully changes.

### **Legislatures and electoral systems**

With the demise—gradual or otherwise—of monarchical government, parliamentary legislatures emerged from the shadow of the executive. With the rise of the modern

political party, those legislatures may be said to have retreated back under that shadow. The deliberative and hence policy-making role of the modern parliamentary legislature is greatly limited by the grip of party discipline and the weight of executive dominance. In the American presidential system, by contrast, an independent and powerful legislature retains an undeniable policy-making role. In both parliamentary and presidential legislatures, committee systems are an important mechanism for legislative deliberation. However, committees play a far more powerful and prominent role in Congress than they do in parliamentary legislatures, shaping the legislative agenda in a way that the executive does in parliamentary systems. Congress has maintained the position the founders envisaged as an equal partner in government.

The choice of electoral system also has a potentially significant impact. In the British tradition, lower houses—the house in which government is formed—have traditionally been elected on a single-member basis that distorts representation. The single-member electoral system leads to the dominance of two major parties and accentuates the winning margin to create ‘manufactured majorities’. This contributes to executive dominance by facilitating single-party majority government. In the continental European tradition, lower houses are normally elected on a multi-member basis that delivers a high degree of proportional representation (PR). This allows smaller parties seats in parliament and denies winning parties a winner’s premium. It thus generates a reliance on coalition formation or minority government that puts the legislature in a stronger position vis-à-vis the executive.

### **The bicameral legislature**

Parliamentary legislatures also vary considerably in their efficacy and policy



impact depending on the way in which they are constituted. Strong bicameralism—present in such parliamentary federations as Australia and Germany—provides the possibility of a differently constituted second chamber acting as a counterweight to the power of the executive. Second chambers have some potential to arrest the much lamented ‘decline of parliament’. The original logic of bicameralism as a framework for representation by ‘estates’ has of course been nullified by democratisation, but newer rationales have provided ongoing justification.

Federalism is prominent among those rationales and bicameralism is often thought of as intrinsic to a system of divided jurisdiction since it provides the opportunity for dual logics of representation: one house based on the democratic principle of representation by population and one house based on federal principle of representation by region. In practice, though, truly federal bicameralism is so rare as to be virtually non-existent. Indeed, only the German model of a council rather than senate-style second chamber has succeeded in functioning as a States’ house. By contrast with the popularly elected senates of Australia or the United States, seats in the *Bundesrat* are filled by appointed delegates from the State (*Länder*) governments voting en bloc.

The Abbé Sieyès summed up one current of thought about bicameralism when he quipped, in a much-quoted phrase, ‘if the second chamber agrees with the first it is superfluous and if it disagrees with the first it is mischievous’. It could not be said that the good Abbé was erring on the side of caution; and the subsequent path of constitutional government in revolutionary France may well have proved him tragically wrong. Consistent with his view, though, the late twentieth century saw a number of smaller democracies abolish their upper houses and opt for

unicameralism—notably in Scandinavia and New Zealand. Sub-national governments in federal states vary between those where bicameralism has generally or overwhelmingly been retained (US, Australia) and those where it has been entirely abandoned (Canada, Germany).

The contrary view is that bicameralism has a crucial role to play in restraining the impulsiveness of the lower house. For this reason, the American separation of powers doctrine encompassed not just a separation of branches but the further separation of what was regarded as the most dangerous branch, the legislature, into two countervailing houses. Thus, according to Madison in *Federalist* 62, bicameralism “doubles the security to the people by requiring the concurrence of two distinct bodies in schemes of usurpation or perfidy”.

The suggestion that bicameralism is either redundant or obstructive is not generally supported by modern analysis. Even in cases where the two houses are similarly constituted, the necessity for legislation to pass two elected bodies will improve the depth of debate and quality of outcome, it is argued. In those cases where the two houses are differently constituted a further benefit is derived from the need for concurrent majorities that require a broader degree of political consensus for policy decisions. Bicameralism is widely regarded as constituting an important element of modern governance—holding the potential to serve as an avenue for alternative bases of representation; increase the ability of parliamentary legislatures to enforce executive accountability; and raise the consensus threshold.

While entirely consistent with the presidential system, strong bicameralism does not dovetail so smoothly into a parliamentary system. The principle that the executive government answers to the legislative branch

potentially creates awkward situations when the legislature may have one chamber opposed to the government. Much will depend on the precise allocation of powers between the two chambers and the procedures for resolving inter-cameral disagreements and deadlocks. In respect of disagreements, the German parliament's constitutionally-mandated 'mediation committee' stands out as one of the most notable solutions, while in Australia resolution of deadlocks remains a contentious issue after a century and a half of parliamentary bicameralism.

### **Performance implications**

While the presidential separation-of-powers system has its defenders (e.g. Shugart & Carey 1992), it has been subject to a battery of criticisms. An early one was that it is essentially an anti-democratic device designed to frustrate the popular will and protect the interests of privileged minorities. Other criticisms have targeted its tendency to 'deadlock' (Burns 1963) or 'gridlock' whereby policy-making is perpetually frustrated by the continuous need to assemble concurrent majorities and existence of numerous 'veto points' where concentrated minority interests can block majority initiatives and where side payments (the notorious 'pork barrelling') are a permanent feature.

Others have noted that outside the United States, presidentialism has been essentially limited to Latin and South America where it has an extensive but hardly inspiring record—being closely associated with political instability, economic mismanagement, democratic failure and authoritarianism. Such arguments, may be overly reductionistic, neglecting a wide variety of other democratic disabilities that have afflicted those societies. But it may also be that under such unpropitious circumstances, presidential systems are particularly ill-suited. As

summarised by Stepan and Skach (2001:275), "the explanation for why parliamentarianism is a more supportive constitutional framework lies in the following theoretically predictable and empirically observable tendencies: its greater propensity for governments to have majorities to implement their programs; its greater ability to rule in a multiparty setting; its lower propensity for executive to rule at the edge of the constitution and its greater facility at removing a chief executive who does so; its lower susceptibility to military coup; and its greater tendency to provide long party-government careers, which add loyalty and experience to political society." Persson and Tabellini (2003:274) have also found that "presidential regimes are associated with significantly worse economic performance".

A different approach draws a contrast not between parliamentary and presidential systems *per se*, but between 'consensus' and 'majoritarian' systems. Majoritarian systems are those that deliver power into the hands of a winning plurality or majority — regardless of how small that plurality is. They then function on an adversarial basis pitting government against opposition. Consensus systems set a higher threshold, requiring a larger majority, and function on a more inclusive and negotiated basis. Britain's Westminster version of parliamentary government has long epitomised crude majoritarianism. At the same time, though, the US presidential system also has some decidedly majoritarian characteristics, notably in the design of its executive branch and electoral system.

Which approach is better? Does it make any difference? Lijphart (1999) is representative of a school of thought that says it does indeed make a difference and that both democratic quality and policy performance are demonstrably better in consensus systems than in majoritarian ones. The decisive independent variable turns out to be the

electoral system. The most consensual and successful democracies are those that are parliamentary and based on proportional representation. The evidence suggests that greater policy stability and a stronger basis of consent produce superior economic outcomes on important indicators such as inflation and unemployment. It must be noted, though, that such assessments are fraught with methodological problems of multivariate comparison, problems that could quite easily vitiate the conclusions (Anderson 2001).

### **Policy implications**

The contrast between systems that concentrate powers and those that separate them has also been of considerable interest to the positive science of politics. In the theoretical tradition of institutionalism, the comparative study of public policy focuses on the ways in which the system of government shapes outcomes by the incentive and possibility structures it creates. At the very least, a highly fragmented system with numerous veto points can be expected to retard policy making, dampening both innovation and retrenchment. This leads to the possibility of game theoretic analysis exploring the impact of varying incentive structures on the dynamics of individual and collective action (Tsebelis 2002).

While parliamentary systems with numerous veto points exist, no system better exemplifies such an arrangement of institutional obstacles than the presidential system of the United States — particularly given the reinforcing effect of federalism. An extensive literature in the tradition of historical institutionalism looks to the highly fragmented nature of the US political system to help explain ‘American exceptionalism’ in such important areas as social policy and tax policy (e.g. Orloff 1993; Steinmo 1993; Finegold and Skocpol 1995; Steinmo and Watts 1995; Noble 1997; Boix 2001).

### **Conclusion**

Conceptually and historically we are able to distinguish between three different ‘branches’—legislative, executive, judicial—according to their respective roles in a system of representative government. In principle, we identify parliamentary systems as those systems of democratic government where the legislative and executive branches are fused, and presidential systems as those where the executive is separate and independent. In practice there are enormous variations in the way the three branches are constituted and combined. At the Westminster extreme of parliamentary sovereignty, they came to be tightly fused. At the Washington extreme the entire system was designed to embody the separation of powers whereby three powerful branches would be forced to work in union while being quite distinct. Having emerged from the American model, the principle and practice of a separate judicial branch empowered to review the constitutionality of legislative and executive actions has become a pervasive and indeed almost defining feature of liberal democracy.

Developments in the latter half of the twentieth century have seen much greater diversity in legislative–executive structures emerge. Finland pioneered the mixed model whereby the parliamentary principle of a political executive based in and answerable to the legislature was combined with the presidential principle of a ‘chief executive’ wielding significant powers, a model that attracted much greater attention when the French reverted in 1958 to that more monarchical form. Variations of the mixed model are now pervasive among the large number of new democracies where the realities of strong leadership must be accommodated within constitutional systems.

Ongoing analysis and debate focuses on the performance implications of competing

models. The way the three branches are constituted in any system of government may well have implications for the quality of representation and governance, and following on from that the quality of economic management. Democratic systems are expected to meet a range of expectations, not all of them easily reconcilable, among them: representativeness, accountability, efficiency and efficacy. The separation of powers doctrine was developed and applied as the most celebrated means of achieving some of those aims, but whether it does so effectively, or does so without defeating others, remains a subject of debate.

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## Libertarianism

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The word “libertarian” combines the word “liberty” and the suffix “-ian”, literally meaning “of or about freedom.” It is an antonym of “authoritarian,” and the simplest dictionary definition is “one who advocates liberty” (Simpson & Weiner 1989). But the name “libertarianism” has been adopted by several very different political movements. Property rights advocates have popularized the association of the term with their ideology in the United States and to a lesser extent in other English-speaking nations. But they only began using the term in 1955 (Russell 1955). Before that, and in most of the rest of the world today, the term has been associated almost exclusively with leftists groups advocating egalitarian property rights or even the abolition of private property, such as anarchist socialists who began using the term nearly a century earlier, in 1858 (Woodcock 1962:281).

This entry distinguishes between three types of libertarianism: left, right, and socialist. It then considers the extent to which the policies of these three diverse groups overlap. The third section focuses on the policies of right-libertarians, both because they have popularized their association with the name and because they have a more unified policy agenda.

### **Libertarianism: Left, Right, and Socialist**

At least three distinct groups claim the name “libertarian” today. There is no clearly agreed terminology to distinguish the groups but the terms “left-libertarian,” “right-libertarian,” and “libertarian socialist” suffice. The three are not factions of a common movement, but distinct ideologies using the same label. Yet, they have a few commonalities.

**Libertarian Socialism:** Libertarian socialists believe that all authority (government or private, dictatorial or democratic) is inherently dangerous and possibly tyrannical. Some endorse the motto: where there is authority, there is no freedom.

Libertarian socialism is also known as “anarchism,” “libertarian communism,” and “anarchist communism.” It has a variety of offshoots including “anarcho-syndicalism,” which stresses worker control of enterprises and was very influential in Latin American and in Spain in the 1930s (Rocker 1938; Woodcock 1962); “feminist anarchism,” which stresses personal freedoms (Brown 1993); and “eco-anarchism” (Bookchin 1997), which stresses community control of the local economy and gives libertarian socialism a connection with Green and environmental movements.

Modern libertarian socialists include Noam Chomsky (2003, 2004), Murray Bookchin (1986, 1997), Sam Dolgoff (Dolgoff 1986), Daniel Guérin (2005), Colin Ward (1973), and George Woodcock (1962). They take their defining influence from the early socialists who split from the Marxists because of their opposition to the authoritarian aspects of the dictatorship of the proletariat. These thinkers include Pierre Joseph Proudhon (1994), Michael Bakunin (1972), Peter Kropotkin (1995), Rudolf Rocker (1938), and Emma Goldman (1911). To some extent anarchist forbearers also include Max Stirner, Leo Tolstoy, George Orwell, Bertrand Russell, and the early liberal tradition (Woodcock 1962), although some anarchists are hostile to what could be called “bourgeois liberalism.”

A guiding principle of libertarian socialism is that all people must have the equal privilege to share in the blessings of liberty, and this principle leads to opposition to unequal property rights. They want to replace the state and the capitalist property

rights regime enforced by the state with voluntary mutual aid associations made up of free individuals. They consider centralized authoritarian socialism, such as the regimes that took power in Russia and China, to be another form of state oppression.

Anarchists are a diverse group who put great stress on individual initiative and action. Therefore, it is hard to determine the libertarian socialist position on many specific issues. Some libertarian socialists oppose political action to further social reform within the prevailing system of government authority, and prefer only direct action that works outside of government authority. All libertarian socialists want radical social reform and the fewest possible restrictions on human behavior. All want to end the state and private property as we know them, and replace it with some kind of non-hierarchical decentralized coordination system that allows for voluntary mutual aid so that all people have the same access to use the means of production toward their own ends (Bookchin 1997, Chomsky 2003, Heider 1994, Rocker 1938, Woodcock 1962).

The question of how this is to be done has nearly as many answers as there are anarchists. Some want worker control of factories. Some want community control of local economies. Some place great stress on gender and ethnic equality, sexual freedom, and personal and cultural freedom. Some place great stress on environmental protection. Some see worker control and economic equality as the primary means of establishing most other kinds of personal freedom.

Libertarian socialist action today is embodied in the creation of nongovernmental organizations and networks aimed at mutual aid and sharing. Communes in rural and urban settings around the world are a form of anarchist action. Workers cooperatives, such as the Mondragon in Spain, further a

libertarian socialist agenda, as do consumer cooperatives. The sharing of software and information on the internet can be seen as a libertarian direct action.

Libertarian socialists have succeeded in having some influence over left-of-center economists who are more closely associated with Marxian economics. For example, Samuel Bowles, David Gordon and Thomas Weisskopf (1983:261-290) propose “An Economic Bill of Rights,” which is not strictly libertarian socialist because it works within existing state structures. However, its content—including rights to a democratic workplace and democratic rights for the people to chart their economic futures—incorporates much of the libertarian socialist agenda.

**Right-Libertarianism:** Right-libertarians believe in strong private property rights and/or an unregulated market economy with little or no redistribution of property. They are also known as “free-market advocates,” “property rights advocates,” or “Neoliberals.” The most extreme version of right-libertarianism, termed “anarcho-capitalism”, advocates virtually unlimited private property rights. Right-libertarians seldom call themselves right-libertarians, preferring to call themselves simply “libertarians,” often denying any other groups have claim to the name. It is perhaps poetically appropriate that property rights advocates have appropriated a term that was already being used by people who subscribe to the idea that property is theft, and that these property rights advocates now accuse anarchists of trying to steal it from them.

Modern right-libertarian thinkers include a large number of economists, philosophers, and political pundits, such as Milton Friedman (1962, 1980), James Buchanan (1975), Robert Nozick (1974), Eric Mack (1990, 1993, 1995), Jan Narveson (1988,



1998), Israel Kirzner (1981, 1989), William Niskanen (2003), Murray Rothbard (1978, 1982), and Michael Tanner (1996). They take defining influence from such thinkers Ludwig Von Mises (1927, 1949), F. A. Hayek (1944, 1960), and the later writings of Herbert Spencer (1872, 1901). They sometimes call themselves “classical liberals” and claim to be the heirs of early liberals such as Thomas Hobbes (1962), John Locke (1960), Adam Smith (1776), and John Stuart Mill (1859). However, the modern right-libertarian defense of private property is so radical as to be in opposition to the views of property held by nearly all classical liberals, and some liberals argue that right-libertarianism has strayed from the essential characteristics of liberalism (Freeman 2001).

Most right-libertarians use an ethical argument based on natural property rights to support their market policy prescriptions. Right-libertarians promote liberty as negative liberty or freedom as noninterference (Berlin 1969). That is, a person is free to do whatever no other person prevents her from doing whether or not she is actually able to do it. In the sense, a person is free to fly by flapping her arms even though she is unable to do it. Right-libertarian freedom is also often expressed as self-ownership—the belief that every adult individual owns herself and no one can take away her rights over herself away without her consent (Cohen 1995, Locke 1960, Nozick 1974, Otsuka 2003). Self-ownership does not mean that people naturally treat themselves as property; it means instead that every individual is free from being treated as the property of another person. A self-owner determines what he or she will do.

Although libertarian socialists and right-libertarians agree about their skepticism of state authority, they have diametrically opposite views of property. Libertarian socialists oppose state authority largely

because they see it as the source of property rights; right-libertarians oppose state authority because they see it as the enemy of private property rights (Heider 1994:95). Right-libertarians combine the belief that all individuals have strong self-ownership rights with the belief that individuals have the responsibility to respect preexisting claims to private property in natural resources even if these claims are unequally and unfairly divided. According to right-libertarians, unowned natural resources are essentially up for grabs. But once someone appropriates them as private property, the owner’s rights are extremely strong and ever lasting. Owners have little or no responsibility to share with those who have no property. In some right-libertarian theories, individuals’ claims of property ownership are as strong as individuals’ claims of self-ownership (Feser 2005, Narveson 1988, Nozick 1974, Wheeler 2000). In contrast to the views of libertarian socialists any attempt by the government or any other authority to ensure that everyone has access to property is unjustified interference with the natural right of property. Government authority, if it should exist at all, must be limited to protecting property and self-ownership rights.

The term right-libertarian also applies to those who believe that the government should be similarly limited for pragmatic or utilitarian reasons, although this is usually considered to be a less important argument for right-libertarianism policies. Unlike libertarian socialism, which leads to diverse political objectives of its adherents, right-libertarianism is easily identifiable with moderate and strict policy prescriptions on nearly all issues.

**Left-Libertarianism:** According to Peter Valentine (2000), left-libertarians combine a belief that all individuals have the right to strong self-ownership with a belief in some

kind of egalitarian right of ownership of natural resources. They share the belief with libertarian socialist that an equal right to be free implies an equal right of access to (or ownership of) natural resources (Gibbard 2000, Otsuka 2003, Steiner 1994, Vallentyne 2000), but they propose a more individualist solution. Rather than wanting to abolish private ownership of property, left-libertarians want to equalize private holdings of natural resources, or at least tax private holdings of natural resources in some way to ensure that all individuals have equal access to their benefits.

Use of the term “left-libertarian” for this group in particular is slightly overly specific because libertarian socialists are also on the left of the political spectrum. The term “left-libertarian” is sometimes used as a generic term for the two groups of libertarians on the left. However, “left-libertarianism” is mostly commonly used for the combination self-ownership with resource equality, and it is what this group usually calls itself, while the other main group in the libertarians left more often use the terms “libertarian socialist” or “anarchist.”

Left-libertarians take their defining influence from thinkers such as Thomas Paine (1797), Thomas Spence (1793), the early writings Herbert Spencer (1872), Henry George (1976), and Leon Walras (2000 [1896]). They take a great deal of influence from the early liberal movement and some influence from both of the other two libertarian movements. Modern left-libertarian thinkers include Hillel Steiner (1992,1994), Michael Otsuka (1998,2003), Peter Vallentyne (2000,2003), Nicolaus Tideman (1982, 2000, 2004), and Philippe Van Parijs (1995). The term, “Georgist” refers to a subset of left-libertarians who accept Henry George’s positive economic theories about the efficiency of a land tax and the causal role of rent in the business cycle

(George 1976), but most left-libertarians are not Georgists and they tend to consider their ideology as primarily normative. There is a connection between some forms of left-libertarianism and Green, environmentalist, and libertarian socialist ideologies, but many of these groups do not accept the left-libertarian thesis of self-ownership.

Left-libertarians, like libertarian socialists, are such a diverse group that it is hard to define the left-libertarian position on many issues. However, unlike libertarian socialists, left-libertarians are largely defined by one policy issue. Although they differ on how resource equality should be achieved and on what resources should be equalized, they are united by the search for some version of resource equality.

The best known left-libertarian policy prescription is the belief that the government must tax away 100% of the resource value of land and other fixed assets, and every individual is entitled to one share of whatever benefits are derived from that revenue (George 1976, Paine 1797, Steiner 1994). Property holders would pay a tax to the state equal to the rental value of a vacant lot on the site of their property. For these left-libertarians, the private individual or business attains the right to hold a natural resource by paying the full market value of the resource in its raw state to the government as representative of everyone else, but the value of the efforts and improvements they put into their holding are private property at least for the life of the owner. This form of left-libertarianism leads essentially to a market economy on stated-owned, privately rented land.

Left-libertarians do not necessarily agree about what the government should do with the revenue from such a tax. Some believe that it should be used for public purposes, such as defense, police, courts, parks, healthcare, and anything else that benefits the

community (George 1976, Steiner 1994). Others argue that it should be redistributed in cash as a basic income—a cash income unconditionally paid to everyone (Steiner 1992, Van Parijs 1995). Under the equal-shares version, each person receives one share of the rental price of all natural resources in cash, as if she owned one share in a giant real estate holding firm that distributed all of its profits in dividends. Others argue that an equal claim to natural resources exists, but it confers only the right to *work* with resources or the right to employment (Van Donselaar 2003).

Left-libertarians disagree about when to stop taxing. Some believe that although it is imperative that the government tax 100% of the land and natural resource rights, respect for self-ownership prohibits almost all other kinds of taxation, most especially income and sales taxes (Vallentyne 2007). However, most argue that inheritance should also be taxed either because assets are abandoned at the point of death (Steiner 1992), or because there is nothing a person or a group can do to impose their claims to any asset on future generations (Widerquist 2006). Others add taxes on monopolies and income derived from any market disequilibria, such as efficiency wages and insider advantages (Van Parijs 1995).

The basic left-libertarian judgment about resource ownership could be paired with any other type of policy. Some left-libertarians appear otherwise very close to right-libertarians; others consider themselves to be both left-libertarians and libertarian socialists. Philippe Van Parijs uses left-libertarian premises in an argument for an extremely activist welfare state (Van Parijs 1995).

### **Common Policies?**

Although all three movements have roots in the liberal tradition, they do not stem from a common branch off of that tradition, and

there is a great deal of mutual animosity at least between right-libertarians and the other two groups. Perhaps Max Stirner (1845) is common to the three movements, but he is not a central figure for any of them, and some in each group would deny his influence. As different as these groups are, they do have some beliefs in common. They all put a high priority on protecting their (conflicting) conceptions of liberty, and they are all skeptical of authority. All advocate strict limits on government authority, sometimes to the point of advocating its complete abolition.

**Tendency to Anarchy:** Neither anarcho-syndicalists nor anarcho-capitalists see the absence of government as the absence of coordination. Anarcho-capitalists, led by Murray Rothbard (1978), see anarchy as a private property economy in which owners protect their property with private security forces hire private arbitrators to settle their disputes rather than relying on government courts. Anarcho-syndicalists and eco-anarchists see anarchy as the breakdown of government protection of property rights. Workers take control of factories, or neighborhoods take control of the local economy, eliciting only voluntary participation from individuals (Bakunin 1972, Goldman 1911, Guerin 2005, Rocker 1938).

**Deference to Individual Choice:** Left- and right-libertarians endorse J. S. Mill's harm principle as the guiding principle of government (Mill 1859). Enforceable duties can be summarized as one duty not to harm each other. The sole justifiable use of government's coercive power is to defend individuals from harm imposed by others. Because left- and right-libertarians posit very different property rights, they have very different conceptions of what constitutes harm, and the similarity in how they apply this principle is limited, and applies mostly to

areas in which property is not directly involved.

Libertarians of all stripes tend to defer to individual choice and oppose laws motivated by paternalism, laws that require one person to actively aid another, and laws that are designed to promote a particular kind of lifestyle. Anti-paternalism implies opposition to drug prohibition and to individual safety regulations such as seatbelt and helmet laws, and to sin taxes such as alcohol and cigarette taxes to the extent that those taxes are designed to protect the consumer from harming herself rather than to prevent the consumer from imposing harm on others.

Prohibition of forcing one person to actively aid another implies opposition to the military draft and possibly to mandatory voting, jury duty, and Good Samaritan laws. Right-libertarians and libertarian socialists have worked together against war and the military draft (Heider 1994:93-94).

Right-libertarians believe redistributive taxation constitutes forcing one person to aid another, but left-libertarians and libertarian socialists believe that unequal property rights in natural resources without compensation constitute forced aid *from poor to the rich*. They believe collective ownership of resources (and perhaps the means of production) gives them great leeway to make sure that no one is needy without forcing anyone to aid anyone else. A few right-libertarians have give tentative approval to the idea that taxation of resources as at least more acceptable than other forms of taxation (Pollock 1996).

Neutrality between lifestyles implies a very liberal outlook on social issues. Minorities as defined by sexual orientation, ethnicity, religion, and politics must have the same access to public facilities and the same rights of free speech, contract, freedom of expression as everyone else. Even some right-libertarian think-tanks have come out for gay

marriage (Epstein 2004). However, right-libertarian defense of property often allows private discrimination. The business owner's right to property entails the right to refuse to do business with anyone else even if that decision is based on bigotry (Murray 1997). Similarly, all three groups tend toward unconditional defense of free speech, but many right-libertarians believe that employers may discriminate against employees based on their speech, their political activities, or any other reason they choose.

**Child Protection:** Anti-paternalism applies only adults. With the exception of the most radical right-libertarians most libertarians accept that the government or the community has a role in protecting children, which can include protection against child abuse, prohibitions on child labor, mandating education attendance. However, libertarians would argue that the government should defer to parents unless there is strong evidence of wrong-doing. Rather than publishing a list of regulations for how all parents should behave, government protection of children should be limited to protecting children from clearly unfit parents.

**Abortion:** Abortion divides libertarians as much as it divides everyone else. Some libertarians view the prohibition of abortion as one group's attempt to force their lifestyle on other groups. Other libertarians, particularly right-libertarians, claim that the fetus's right to self-ownership implies that all abortion must be illegal (Gordon 1999). However, a self-ownership argument can be made in the opposite direction. That is, a prohibition on abortion amounts to forcing the pregnant woman to aid the fetus against her will, violating her self-ownership (Narveson 1988, Thomson 1971).

Most libertarian socialists believe that no government authority has the right to prevent

a woman from having an abortion, but some more radical anarchists believe that instead of taking political action in favor of legal recognition of that right, an individual's time would be better spent helping women obtain abortions, or working to subvert a government that assumes overreaching authority.

**Immigration:** The three groups of libertarians tend to support open immigration but for slightly different reasons. The left-libertarian and libertarian socialist belief in egalitarian ownership of the Earth makes it difficult to exclude anyone from immigration. However, left-libertarians might believe one nation can exclude immigrants as long as individuals on both sides of the border have equal access to the use of (or the value of) the world's resources. Some libertarian socialists have been known to give aid to so-called illegal aliens.

Right-libertarians could say that one group of people has a right to certain land, and another does not, but under right-libertarianism nearly all rights occur at the individual level. Therefore, if any one person within a nation wants to hire, or rent a dwelling to, a foreigner, no one else has the right to interfere. A few libertarians have found excuses to overcome this implication of their principles (Hoppe 1998), but most do not (Block & Callahan 2003).

### **Right-Libertarian Policies**

Even within right-libertarianism, there is a large disagreement about how minimal the minimal state should be. The most extreme version, anarcho-capitalism, is discussed above. More commonly, however, right-libertarians argue for the minimal taxation necessary to support the protection of self-ownership and property ownership (Narveson 1988, Nozick 1974). This version of the right-libertarian government is often called the

“night watchman state,” because the government is essentially limited to a security role. It can justifiably tax individuals to support police, courts, defense, and not much else. However, there is some difficulty in determining exactly what level of spending on police, courts, and defense constitutes the minimum necessary to defend individual rights. A large part of the military budget, especially in a powerful nation such as the United States is not strictly limited to defending the nation from invasion. Many people who otherwise espouse right-libertarian economic policies also espouse hawkish military policy, but the right-libertarian position is for a small military that does only the minimum necessary to defend the nation from attack, and only that which is genuinely in the interests of the vast majority of individuals (Rothbard 1978).

Of course, even the functions of defense, police, and courts are justified by the market's failure to deliver these goods without government intervention (Nozick 1974). But market failure arguments exist for almost anything an activist government might want to provide including public parks, roads, and highways; libraries, the post office, public education; healthcare; regulation of industry; social safety nets; and breaking up monopolies. Thus there are many different kinds of right-libertarianism depending on where and how one draws the line of a market-failure argument for government action. Some make strict rights-based arguments against nearly all government action (Narveson 1988, Rothbard 1978), and others merely look for market-based solutions to popular government goals (Friedman 1962, 1980).

**Redistribution:** While a radical change in the property rights regime is essential to left-libertarianism and libertarian socialism, it is anathema to strict right-libertarianism for

reasons discussed above. However, some right-libertarians have given provisional support to limited redistribution of income either for practical or charitable reasons or because they see it as a political inevitability. There is some connection between the three libertarian groups in the strategy for redistribution. Right-libertarians who accept redistribution tend to favor some kind of basic income or negative income tax (Friedman 1962, 1968, 1980; Hayek 1956; Murray 2006; Steiner 1992; Van Parijs 1995), as do some left-libertarians (Steiner 1992, Van Parijs 1995), and some elements in the libertarian socialist movement (Heider 1994:66). The libertarian appeal of basic income is that it is a simple policy that is minimally intrusive in the lives of the poor. The government doesn't hire a large number of administrators or social workers to supervise the poor or the find work for them, it simply transfers money from one group to another.

**Education:** A strict right-libertarian education policy would be none at all except perhaps a law mandating that parents find some way to educate their children. However, given that mandatory public education is so overwhelmingly popular many right-libertarians have searched for a market-based policy that achieves public education's goal. In 1962, Milton Friedman proposed a "voucher plan" for schools in which parents would receive a certain amount of money from the state that could be used at any private or parochial school whether for profit or not (Friedman 1962). Although the state still pays for education, this program is right-libertarian in the sense that parents would have a choice in a market of schools. Although this program has not been fully implemented in any jurisdiction, elements of it have been incorporated into "school choice" initiatives around the United States and the world; something like it exists in the

Netherlands; and the idea continues to gain momentum among right-libertarians and conservatives (Enlow & Ealy 2006, Salisbury & Tooley 2005).

**Healthcare:** Although economic theory has produced strong arguments for the existence of market failure in the healthcare industry, and although others see a strong equity argument for free healthcare, a strict right-libertarian policy would be to remove all government involvement from the industry by deregulation, ending special tax deductions for medical benefits, and ending government programs such as nationalized healthcare in most of the developed world and Medicare and Medicaid in the United States. Individuals would then have to try to solve the market failure problems without government assistance, and those who cannot afford it would seek it through the charity of the wealthy. However, if that is not politically feasible, right-libertarians such as Charles Murray have proposed something like Friedman's voucher plan for healthcare. Murray proposes that the government give each individual \$3,000 per year that she must spend on health insurance in a heavily deregulated market (Murray 2006). Thus, the government would pay for everyone's basic healthcare, but consumers would have a choice in a market for health insurance.

**Macroeconomic Policy:** Right-libertarians tend to advocate (small c) conservative macroeconomic policies. A few go so far as to say that the government should privatize the central bank or return to a gold standard, but most accept the argument that a familiar state-run central bank is necessary. However, right-libertarians argue that the government should not pursue an activist counter-cyclical monetary policy but should aim for a stable money supply (Friedman & Friedman 1980; Friedman & Schwartz 1963).

Most right-libertarians wish for a government that is too small to make a counter-cyclical fiscal policy a realistic possibility even if it were desirable. The usual right-libertarian solution to recessions is to avoid causing them by sudden shifts in government monetary and fiscal policy, by removing government barriers to market functioning, and by letting the economic cycle work itself out. Often right-libertarians see the business cycle as part of the natural course of economic growth, which cannot be stopped without reducing its long-run benefits. According to right-libertarians, the best solution to unemployment is to remove government programs such as labor regulations, health and safety regulations, unemployment insurance, and minimum wage laws, all of which they see as something that might prevent firms from hiring as many workers as they might otherwise.

**International Trade:** Right-libertarians tend to favor free international trade and to support the unilateral elimination of all tariffs and quotas on imports and all subsidies for exports. The usual nationalistic arguments for government protection of home industry (such as self-sufficiency and support of local industries or wage rates) all oppose right-libertarian principles of property ownership and free exchange. However, more recent arguments for international trade restrictions have the potential to justify them on libertarian terms. Thomas Pogge (2002), for example, argues that much of the industrialized world's trade with lesser developed nations is not characterized by the free exchange of property between rightful owners. Many lesser developed countries are run by dictators who essentially use government authority to steal property from their citizens and sell it to the corporations of the industrialized world. This argument seems to make a libertarian case for restricted trade

with (or even an embargo of) undemocratic countries, but the argument does not seem to have penetrated right-libertarian circles. The more common right-libertarian view of international trade is that commerce with any nation is good and it will eventually benefit everyone.

**Is Right-Libertarianism Right-Wing?** Strict right-libertarian policies on economic inequality, healthcare, education, and other issues give it an elitist, right-wing character, and justifies the rightist designation. However, some right-libertarian policies are clearly distinct from right-wing conservatism. For example, Murray Rothbard is highly critical of militarism and the war on drugs, "That is a beautiful war, because they can never win it. It is a perfect war from the point of view of the state" (Interviewed by Heider 1994:95). Many of Rothbard's followers would say the same about the war on terrorism.

Policies in which strict right-libertarianism conflicts with conservatism include not only the social policies they share with the libertarian left but also many right-libertarian economic policies. For example, some American conservatives espouse right-libertarian rhetoric to argue against government subsidies for passenger rail, but right-libertarianism, consistently applied, would actually lead to an enormous expansion of passenger rail at the expense of most other forms of transportation, which receive enormous government subsidies. Not only would the government have to stop subsidizing jet fuel, it would also have to sell government owned airports and the air traffic control system. Indirect automobile subsidies would also have to go, including free roads, streets, highways, public parking, and traffic lights, not to mention direct subsidies for oil drilling, for pipelines, and for dictators in oil-producing nations. A few right-libertarians

make a strange exception by supporting the government provision of roads (Murray 1997), but most libertarians believe that it is no more reasonable for a government to provide a free road to every person who wants to drive a car on it, than it is to provide a free rail line to every person who wants to drive a locomotive on it.

Part of the reason right-libertarianism is considered a right-wing doctrine is the alliance between right-libertarians and religious and authoritarian conservatives in the Republican Party in the US. Many people espouse right-libertarian arguments against the redistribution of income, minimum wages, and government regulation of industry while simultaneously espousing distinctly un-libertarian arguments on issues such as gay rights, drugs, religion, militarism, and free expression. This view could reflect a willingness among right-libertarians to sacrifice these issues to find allies on their most cherished economic issues, or it could reflect the appeal of right-libertarian economic ideas with conservatives. Of course, the combination of market economics with social conservatism (Gilder 1981; Mead 1986, 1992, 1997) is an ideology of its own, which seems to be coalescing under the name of “neo-conservatism;” it is not, however, a form of libertarianism.

## **Histories**

For history and interpretation of liberalism see Freedman (1996), Gaus and Courtland (2003), and Manet (1994). For the history and philosophical foundations of right-libertarianism see Boaz (1997), Machan (1974, 1982), and Vallentyne (2006). For the history of left-libertarianism see Vallentyne and Steiner (2000); for the philosophical debate between left- and right-libertarianism see Vallentyne and Steiner (2000b). For the history of libertarian socialism see Guérin

(2005), Nettleau (1996), Ward (2004), and Woodcock (1962).

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## Market Socialism

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### **Introduction**

Market socialism, as the name implies, is a combination of a market system and socialist principles. Market socialism is concerned with the optimal combination of centralisation and decentralisation, of markets and planning, of individualism and the common good, and of public and private property. Market socialism is distinct from other economic systems due to its different goals that the system wants to achieve: prevent exploitation, reduce alienation, greater equality of income, wealth, status and power, and the satisfaction of basic needs. These goals can only be realised through the establishment of a socialist economic system, according to market socialists, because the negative outcomes of the capitalist system are inherent, and cannot be avoided merely by using the discretionary power of the state.

### **History of Market Socialism**

Market socialism is not a homogenous theoretical abstraction but rather a number of variants exist under the basic definition. Yunker (2001:1-34) distinguishes between the following theoretical constructs of market socialism:

a) Langian socialism: aims at a socialist equivalent to perfectly competitive capitalism. Today, Lange and Taylor's (1939) contribution to the theory of market socialism is considered archaic because it ignored incentive issues (Roemer and Silvestre 1993:108).

b) Service socialism: aims at replacing profit maximisation with constraint output or revenue maximisation, subject to an additional constraint of making a minimum

(often zero) level of profit. The firm will have to cover its costs and avoid losses.

c) Co-operative or self-managed socialism: aims at installing the employees as the managers of the enterprise. Effectively, enterprises are governed by its employees for the benefit of the employees.

d) Pragmatic socialism: aims at a socialist "equivalent" to contemporary real-world capitalism, with the exception that the reward to state-owned resources will be distributed equally among the general population.

Market socialism in its "pure" form does not and did not exist anywhere in the real world. It is only a model that it has been proposed for possible future social development. However, "approximations" to real world examples can be identified as:

#### *Yugoslavia*

After the Stalin-Tito break the Yugoslav Communist Party searched for an alternative to the command economy to achieve greater efficiency. This was found in self-management with the establishment of the Basic Law on the Management of State Industries by Work Collectives. Based on this law each enterprise had the right to handle its own affairs through elected workers councils, elected management board, and an appointed manager. As self-managed firms had to be autonomous this required the replacement of the command system by full market relations. However, the model was not applied consistently and it was one of the factors that led to the break-up of Yugoslavia.

#### *Liberman-Kosygin Reform*

Acceptance of much of the criticism of the Stalinist model, in the Soviet Union, particularly relating to the economic structure, resulted in the Liberman-Kosygin reform. The Soviet's interest in reform was focused only on changing the economic structure. The extension of market relations

was perceived as a positive factor in reducing some of the weaknesses of the Stalinist model. The aim of partial decentralisation through market relations was to reduce the administrative burden, improve the quality of information and strengthen motivation. The Liberman-Kosygin reform was not successful, because it was not all embracing. In the absence of openness and democracy, the people were unaware of the social reality that existed. The bureaucracy was able to reverse the reform without being subject to any effective opposition.

### *China*

The mechanism chosen and implemented in China was the two-track system. Under this system, there were centrally specified input and output quotas, within which sales and purchases were centrally directed at low prices, which were controlled. Above these quotas, and for production sectors for which did not have quotas, firms producing outputs and inputs were allowed to set prices for their products according to market conditions. This formally established the double-track price system: the co-existence of centrally determined prices and market-determined prices. Today, the balancing act of the Chinese leadership between the revolutionary socialism implemented by Mao Zedong, emphasising public ownership and welfare, mass-based collectivism and egalitarianism, and the market reforms of Deng Xiaoping, with their increasingly capitalistic characteristics, privatised forms of property and class polarisation, have now reached a level of contradiction that must be resolved. Indeed, the analysis of China's "market socialism" reveals that the dynamic process of change tilts towards market capitalism.

### *Mondragon System of Cooperatives*

While the aforementioned experiments took place in socialist countries, in the case of

Mondragon co-operatives in the Basque country of Spain they were nurtured within capitalism. Mondragon co-operatives which extend worker ownership and management in production organisations in association with co-operative educational, banking and commercial institutions questions the neoclassical time-honoured assumption that co-operatives are doomed to failure. The objectives of the co-operatives are the creation of wealth as well as the development of participation and democracy amongst their members (Bakaikoa, Errasti and Begiristain 2004).

Hence, the theory and practice of market socialism is still being developed (Roemer, 1994c:3,290). The market socialist model developed in this paper is an amalgamation and a stylised version of the work of a number of socialist economists.

### **Role of Markets in Socialism**

Marxism is derived from the works of Karl Marx, and it forms the basis for the economic analysis used by market socialists. Marxism has always been central to the construction of democratic and egalitarian alternatives to capitalism, as well as egalitarian reforms of capitalism itself. Market socialists highlight the need to incorporate power and class into economic analysis and believe that these result from the private ownership of the means of production. Markets distribute income according to relative power, not only as a result of productivity.

Marx was silent about the construction of socialism and what socialism specifically involved. Marx declined to write recipes for the social cookbooks of socialism. So some socialists believed that the economic institutions and processes of socialism will emerge naturally and spontaneously; consequently, they do not require serious forethought. Marxian economics is a broad theory of the historical evolution of economic



life. Thus concepts such as “the state withers away” and “the antithesis between physical and mental labour vanishes” do very little to assist socialists in developing a coherent socialist economic system (Howe 1994:53). In the meantime, Marx cannot be blamed for what was subsequently applied as socialism.

Marx ruled out any role for the market in a socialist economy (Roosevelt 1994:123). In contrast, both Bukharin and Trotsky were in favour of the use of “the market evil” (Blackburn 1991b:201-2; Roemer 1994c:3,290; Nove 1987a:31-2). Contrary to Marx, market socialists argue that the market mechanism is the most efficient way of co-ordinating decentralised decision-making. Markets encourage economic innovation in order to produce and distribute the goods that people need for self-realisation. Thus markets can be used to achieve socialist ends (Estrin and Le Grand 1990:1; Roosevelt 1994:136). The market socialists embrace market relations in every aspect of economic life and reject Stalin’s ‘two-property thesis’. According to the two-property thesis, market relations are only legitimate in a socialist system if an exchange of property occurs between participants in the transaction. Between state-owned enterprises there is no exchange of property in any transaction. Thus market relations are not warranted and relations between state-owned enterprises have to be centrally administered (Stalin 1972:1-29).

There is recognition by market socialists that in the market economies market failures exist, in the form of externalities and public goods, economies of scale, unjust distribution of income and advertising (Estrin & Le Grand 1990:4-5). These failures are attributed to market capitalism rather than to markets *per se*: the markets of a socialist economic system need not be anything like the markets of capitalism. Therefore, there is neither a simple-minded endorsement of markets, nor

their straightforward dismissal. Market socialism combines the strengths of the market system with those of socialism to achieve both efficiency and equality. The issue is not whether there are to be markets but, rather, what kind of markets and with what kind of consequences. There is no such thing as a ‘market’: markets are institutionally dependent (Howard & King 1994:140). Markets do not require capitalists or the concentration of economic power and wealth in the hands of a small class. Market socialists attack the ‘anarchy’ of both the market and of central planning. Hence, instead of trying to abolish market relations as an integral feature of socialism and of a Marxist view of socialist transition, socialism should attempt to improve them.

### **Definition of a Good Society**

The market socialist model is concerned with the optimal combination of public and private property, centralisation and decentralisation, of markets and planning and of individualism and the social good. Socialism does not, and will never be able to, abolish scarcity. What socialism offers is a different way of dealing with economic problems: conscious intervention by communal institutions, a ‘visible hand’, and greater social ownership through the reduction of private ownership of the means of production (Bowles & Gintis 1990:41). The call for the abolition of exploitation is a call for an egalitarian distribution of resources, because exploitation is the result of the unequal distribution of the means of production and not of surplus value. Surplus value is the value produced by the worker above the wage rate, which is a characteristic of production processes. But in capitalism, surplus value is appropriated by the capitalist, as a result of private property rights, without an equivalent given in exchange; the capitalist appropriates the results of surplus unpaid labour. In market

socialism, as the majority of property will be in a social form, surplus value will be appropriated by the society and distributed to the members of the society. However, socialism is not only about redistributing income. It is also about designing institutions and relationships which foster independence, self-respect and dignity that give people a greater degree of control over their lives and the capacity to exercise responsibility for their actions. Self-realisation stands for the development and application of individual talents in a direction that gives meaning to a person's life (Roemer 1996:10).

Market socialism is quite different from capitalism in that a market socialist society tries to achieve different goals and a different economic system. For the neoclassical economists, it is utopian to believe that a society can be founded on a norm of egalitarianism. Greed is good, or at least a necessary evil, a motivating force that can be tamed by the right institutions (Roemer 1994a:124). Nonetheless, for neoclassical economists, the dominance of planning questions the ability of the market to function efficiently; planning results in corruption. Meanwhile, Post Keynesian policies of intervention in markets cannot overcome the macroeconomic problems that are rooted in the capitalist system. Economic and political power will tend to undermine the successful implementation of Post Keynesian policies (Elson, 1988, p.21).

Socialism has a well-defined set of ends and values of freedom, democracy, social justice, community, efficiency, self-management, solidarity, preventing exploitation of the weak, reducing alienation, greater equality of opportunity, income, wealth, status and power and the satisfaction of basic needs. Market socialists have traditionally criticised capitalism and Stalinism for violating the central values of equality, democracy, autonomy and

community. This is because capitalist and Stalinist societies are inherently based on domination and exploitation, which heavily influences human relations. Market socialists condemn both capitalist and Stalinist exploitation because they are characterised by unjust inequality of ownership and control of the means of production. The profit incentive system in capitalism and the nomenclature system in Stalinism compel economic actors to treat any other considerations as, at best, secondary. Both economic systems increase inequality of income, wealth and privileges, which affect economic growth and productivity by obstructing the evolution of productivity-enhancing and self-managed governance structures (Bowles & Gintis 1996:309; Bardhan & Roemer 1994:180). These outcomes are due to the highly concentrated private ownership of capital under capitalism and the highly concentrated levels of control and power under Stalinism. In contrast, in market socialism, human needs will be the driving force, not the market or power.

Marx highlighted the inherent tendency of markets to generate exploitation, inequality and instability. Exploitation arises from inequalities in endowments of production, lack of competitive conditions and inescapable market uncertainties (Estrin & Le Grand 1990:14). Even if such sources of inequality were abolished, material incentives, such as rewards in the form of market wages for different skills, will be essential. Inequalities will not be unjust as long as they result from need or merit. Differences in skills result from varying educational opportunities, talents and abilities and the degree of material resources, all of which are attributable to factors for which people have no responsibility. Environmental conditions have to be equalised. As a result, the disadvantaged will be compensated so that people can enter the market on the fairest

possible terms. The overall interest of society cannot just be reduced to a sum of individual self-interests (Brus & Laski 1989:151).

Market socialists aim to rectify market failures in a number of ways (Miller 1990:31-2). Firstly, market socialists endeavour to ensure full employment by the public regulation and democratic planning of investment. As the nature of investment directly determines the level of employment, investment cannot be left to the unstable market forces; societal regulation of investment will ensure the achievement of full employment and a guarantee right to work. Secondly, market socialists strive for a reduction in inequality of income by encouraging the growth of enterprise forms in which primary income is distributed more equally. Enterprises in market socialism will normally take the form of workers' co-operatives, with capital supplied externally and profits distributed equally to the members of the collective (Miller & Estrin 1994:230). Thirdly, market socialists intend to introduce a highly discretionary tax system to facilitate the redistribution of income. Progressive tax on income and wealth and appropriate transfer payments would have reduced inequalities (Yunker, 1997, p.77; Nove, 1989, p.108)

Market socialism provides conscious social direction by combining markets with planning in a way that makes the best use of both instruments. Otherwise the free market will be self-destructive, fostering class differences and promoting a lack of freedom. The market is the only alternative to bureaucracy, and self-management is not in conflict with efficiency. Thus socialism is about equal entitlement to the means of production, with the question of how people choose to use their endowments in the production process left open.

A socialist view of freedom centres on the idea of effective choice. A person who is free

has many options from which to choose, but these options must be real rather than hypothetical. The neoclassical economists accept only a negative view of freedom, which is characterised by an absence of intentional coercion. However, freedom has both a negative and a positive face. Positive freedom is having the ability and hence the appropriate resources to act effectively. The goal associated with market socialism is greater equality at the beginning, so that people entered the market on an equal footing, to achieve the equalisation of positive freedoms in production (Estrin and Le Grand 1990:7-9). This is interpreted in market socialism as embodying three forms of equality: an equal guaranteed basic liveable income; equal access to capital resources; and a limit to market-generated inequalities. In market socialism, "the free development of each becomes the condition for the free development of all" (Roemer 1996b:12). After all, it is the enlargement of freedom which is socialism's highest aim

Consequently, a market socialist economy would combine public ownership of large, established corporations with a high degree of reliance on markets. Market socialists argue that such an economy, in its everyday operations, will appear almost identical to the market capitalist economy of today (Yunker, 1997, p.ix). There will, however, be one critical difference: profits and interest generated by publicly-owned corporations will be distributed to the general public as a social dividend or minimum income supplement to labour income or in the form of lower prices for necessities such as housing, food, electricity, gas etc, instead of being paid out in proportion to financial asset ownership.

### **Institutional Structure.**

Marx emphasised the importance of supporting institutions for accumulation and the fact that institutional choice did not take



place in vacuum. Moreover, given human behaviour, and to ensure socialist outcomes from a market mechanism, the environment will be altered so that market outcomes were consistent with the social interests of efficiency, equity, self-management and solidarity (Howe 1994:72, Nove 1994a:215, Estrin & Le Grand 1990:1, Roemer 1994a:53, Lange 1976:703, Bowles & Gintis 1996:314). The transition to a socialist market would surely require the development of new institutions, possibly no more than those required for the transition to capitalism (Bardhan 1993:154; Bardhan & Roemer 1992:115).

Under market socialism, there would indeed be markets, but there would also be a wide range of other social, political and legal institutions that constrained them. Institutional norms would foster participation in self-management, and the establishment of information disclosure laws, and the institution of periodic “social audit” which monitor infringements of ecological and egalitarian norms (Blackburn, 1991b, p.223). In this context, collusive behaviour and cartels would be illegal (Yunker 1997:170, Howe 1994:73, Nove 1994a:214, Bardhan & Roemer 1992:113). Such institutions could only be the result of targeted societal and state action. Roemer (1996:35) stated that “I remain agnostic on the question of the birth of the so-called socialist person, and prefer to put my faith in the design of institutions that will engender good result with ordinary people”.

### **Political Structure.**

According to market socialists, any reform that requires greater initiative and more personal responsibility in the economic sphere, while maintaining rigid party control over political life, as in Stalinism, simply cannot work. Democratic politics is considerably more important for the success

of market socialist system than it is for the success of a capitalist system. Full and deepened democracy is an essential precondition of socialism (Roemer 1996:32; 1994a:109; Yunker 1986:691). Open criticism, free discussion, differences of opinion and the peaceful competition of interest groups are crucial to any progress, to any meaningful changes in the economic structure toward market socialism. Those who assert a fundamental incompatibility between socialism and democracy normally rely on the association of socialism with the one-party political systems common to all Stalinist countries (Yunker 1986:693).

In a democratic capitalist society, people participate in the decision-making process; however, effective decision-making remains with the capitalists. Democratic affairs in capitalist societies are a matter for specialists, the politicians, and participation in capitalism generates a sense of passivity, isolation and self-absorption inimical to effective democratic citizenship. In addition, majority voting does not lead to efficient economic outcomes. Thus there is no presumption that the capitalist democratic process will result in an efficiency-pursuing government. Reforms will only take place as long as the dominance of the capitalist class is not threatened. The only way that any effective policies in the interest of the majority can be introduced is by eliminating the power of capital. This will require the abolition of private property and its appropriation by the majority of the people: the working class.

Multi-party politics are consistent with socialism, inasmuch as social classes exist in socialism and are heterogeneous. Doing away with political parties results in repression. Conflicts between groups exist, based upon their different economic interests. Under market socialism, there will be several political parties competing for power, and some will be ‘bourgeois’. In the meantime,

democracy is a risky process. Advocates of market socialism recognise the possibility that, if the system did not perform as well as hoped, citizens would have restored capitalism. Then, perhaps, some years later, the socialists might again win the elections. However, socialism will be well embodied in the constitution, which limits the permissible degree of accumulation of private property in productive assets and constitutionally have protected non-private property. The justification for a 'supermajoritarian' requirement to reverse the socialist principles is that the social cost of change will be substantial; changes in property relations should not endanger long-term planning and investment (Roemer 1996:33).

In market socialism, the sectoral and spatial distribution of investment will be subject to both political as well as economic pluralism. The national five-year plan will be based primarily on the plans of the enterprises, which themselves are derived from projected market demand. In addition to taking into account the interdependence associated with investment decisions, the planning process will be a process of debate. Even the greatest precision in the economic calculus will never eliminate the necessity for making political decisions, in drawing up plans of development. It follows that the optimisation of economic decisions embodied not only the system and techniques of economic calculus but also a corresponding political mechanism within which conflicting interests can be clarified and compromised upon. The democratic process itself can help to educate voters as to the real alternatives they face and to engage their cooperation rather than their resistance to the required measures. All will participate in decision-making, so that the decisions taken, in the name of society, are as close as possible to real social preferences.

Plans will be approved by an elected parliament and implemented within market relations mediated by the discretionary power of the state. For the regulation of and application of plans, political pluralism (effective participation of the people) and economic pluralism (market relations) are necessary. A market socialist economy involves a continuing role for the state, one that is much subtler, more indirect and more benign than running an administrated socialist economy. In contrast to central plans under Stalinism, reliance will be primarily on market instruments. Additionally, democracy makes the state's task more difficult, since a variety of inconsistent objectives will be reflected in the preferences of individuals, groups of citizens and political parties' preferences. The trade unions will have an important role as well. They will be more active in participating in the social sections of the plans and even in setting forth their own alternative proposals. Thus market socialism is not a regime of technocrats but a form of economic management that left ample room for pluralism and democratic processes of decision-making.

### **Stabilisation and Investment**

In the market, decisions about whether to invest were extremely complicated. Capital accumulation relies on complex judgements about the likely demand and cost conditions for many years into the future. Decisions have to be based on a balance of expertise, technical knowledge and guesswork. However, the market fails to provide sufficient information to the investor about the future. A set of futures markets, necessary for agents to make suitable contingency plans in times of uncertainty, does not exist in reality (Roemer 1989:160, 1994c:300). This is because it is natural for people to be rather cautious, and also due to the uncertainties in investment being so great; there is a

systematic tendency to under-invest in a market system. Moreover, there is a bias towards projects with fewer uncertainties, risks and, of course, with quick returns. Hence, there is a systematic tendency to under-investment in a market economy, which results in slow pace of growth and constrains improvement in living standards for the population. Playing it safe is of course a characteristic of the banking system, whose role is to fund investment projects. Yet it is often the riskiest projects which drive the motor of economic development. The market socialist state must, therefore, counteract these tendencies by intervening to provide firms with information about the economic environment: prices and market trends. This can be achieved through an indicative plan to foster both the general rate of accumulation and investment in relatively risky projects and plan to innovate for the future as the central authority is qualified to forecast the rate of technological progress. This process is quite similar to the French use of indicative planning however there is a major difference: the dominant form of ownership in market socialism is social and thus there is a guarantee that investment projects will reflect the interests of the society and not short-sighted individual self-interest.

The desired investment levels and pattern of society will be implemented not through a command system but by manipulating the interest rates at which different industrial sectors borrow funds from state banks (Roemer 1991:563, 1994b:271, 1994c:291, 294). Central planning is expected to give way to a variety of forms of market planning. Therefore, only under strong state regulation through planning can the transition to market socialism take place in the form of industry policy. Industry policy is designed to assist enterprises in confronting competitive forces through the provision of information, tax concessions and tariff protection. Industry

policy is designed to stimulate demand and encourage access to capital, skill and infrastructure enhancement to facilitate strategic economic advantage. It encourages enterprises indirectly, through market incentives, to reach a market outcome that is desirable from a societal point of view. Industry policy is essential, market socialists argue, due to the inability of the market system to pick winners.

The plan will determine priorities. It should reflect the priorities of society as a whole and those of the separate social groups whose interests are recognised as being especially important. Prioritising is a complex process and has to be based on social compromise within an open and pluralistic-democratic system. Social and investment priorities are inevitably political decisions for instrumental and desirable reasons. Indicative planning is a decentralised and democratic process of consultation and discussion, concerned exclusively with plan construction and elaboration. The process provides a forum in which information can be pooled. Also, diverse interest groups can confront one another about spillover effects, giving voters an equal voice in determining the plan's objectives. In itself, the plan does not contain an implementation procedure. As every actor 'bargains' through successive 'iterations', the process of negotiated co-ordination, rather than price taking, will occur. Under socialism, the tension between sectional and social interest will be explicit, with the possibility of partial reconciliation and also some transformation of the perceptions and levels of social awareness of those involved.

Under market socialism, capitalist shares and stock exchanges will be removed and the production sector will be financed entirely through a competitive credit market: that is, by a variety of socially-owned financial institutions, state and regional banks, pension funds and philanthropic trusts. However,

those financial institutions with monopoly power will be state-owned. A complex socialist economy will require new types of financial intermediaries, which will be owned by the state if they have market power, to promote greater workplace democracy and to negotiate co-ordination through planning.

### **Property Relations.**

Practically every dictionary defines socialism as public ownership of land and capital (Yunker 1986:680). The market socialists argue that state ownership *per se* does not guarantee efficiency. If the structure of state ownership conflicts with the changing economic realities, state ownership will be a negative rather than a positive element in economic development. State property is no longer considered as sufficient or even necessary for socialism. Within the market socialist economic system, and based on state property, a variety of property forms can exist. Thus all forms of property - individual, co-operative and state - are important and are consistent with socialism (Roemer 1994a:20, Blackburn 1991b:220, Elson 1988:30, Brus & Laski 1989:149).

This argument does not dismiss the role of state property in the socialist economy. State-owned enterprises will be large enterprises characterised by monopoly power (Roemer 1992:262, Yunker 1988:106, 1986:681, Nove 1989:102). State ownership will ensure that the behaviour of large enterprises is in line with the social good. State enterprises will be both instructed and motivated to maximise the long-term rate of profit and thereby also efficiency. Managers of state-owned firms will be induced to pursue profits, not only by making their salaries and bonuses subject to achieved profits but also by threatening job security (Yunker 1997:14). Decision-making in state firms will be based not on the conventional hierarchical structure of firms, but rather on a democratic process in which

all workers participated. For example, in the Mondragon co-operative the board of directors is responsible to the General Assembly and is elected by the members on the basis of one-person vote (Bradley & Gelb 1981:213).

Market socialists argue that co-operatives are consistent with socialist principles (Estrin 1990:166). Enterprises in market socialism will normally take the form of workers' co-operatives, with capital supplied externally (Miller & Estrin 1994:230). Under this structure, ownership and control will be exercised by all members of the co-operative, in the form of group property. All members of the co-operative will be equal, with no distinction between employers and employees and no exploitation of labour. While a hierarchy is necessary for the co-ordination of production processes even in co-operatives, authoritarian hierarchies are not a natural result. There is a positive relationship between participation in decision-making and productivity, as well as between profit sharing and productivity. In firms that allow the workers to make the decisions, the workers can draw from their shop-floor experience to make the correct decisions and respond rapidly. Where work yields utility, and since co-operatives eliminate the exploitation of labour by capital, co-operatives can perform better than hierarchical firms (Estrin & Le Grand 1990:16). In a democratically self-managed enterprise, workers, as a group, have a strong interest in assuring good job performance by monitoring the labour process of individual workers. Empirically, the claim that hierarchical firms necessarily outperform labour-managed firms is yet to be proven.

The new perception of property relations under market socialism goes further than the co-operative form. Private property will be legalised, thereby recognising that it has a role in a socialist system (Yunker 1994:8).

Market socialists will encourage privately-owned firms; however, they will be restricted to small-scale enterprises, with large-scale privately-owned capitalist firms being abolished. Capital will be socialised and rented to firms. Once privately-owned enterprises reach a pre-determined size and gain regional market power, the sole ownership rights of the private owners will be abolished, appropriate compensation paid and the firms transformed into co-operatives. This is analogous to the capitalist entrepreneur, who sells the firm when the owner is prepared to expand the business beyond its small size. But there is one important difference: a capitalist entrepreneur sells out voluntarily to the other self-interested firm wanting to purchase the investment. Under market socialism it will be compulsory, with compensation determined by the state (Roemer 1994c:297). Did the proper compensation for the original entrepreneur result in illegitimate enrichment? No, as long as the socialist market and the price mechanism is functioning correctly. From a societal point of view, there will be no unearned income arising simply from the capitalisation of small ownership of capital and land (Nove, 1994, p.195).

Once co-operatives reach a pre-determine size and gain economy-wide monopoly power, the co-operatives' rights will be relinquished, after appropriate compensation, and their assets transferred to state ownership through legislation (Roemer, 1992, p.271). Market socialists view the property structure of the enterprise as directly linked with monopoly power and the principal-agent problem. While small private ownership of the enterprise will not give rise to power, as the firm grows its power increases, requiring a change in ownership. As the power of the firm increases with its size, ownership will also be altered from private, to co-operative, to state. In this way, no individual or group of

people will gain substantial power in the economy. They will be unable to accumulate substantial wealth, and incapable of influencing economic policy by virtue of their economic control of significant sectors of the means of production. In this market environment, state-owned firms must compete with one another and with cooperative and private enterprises. Thus it will be wrong to conclude from the experience of firms in a command economy that state-owned firms will behave in a similar manner under a market socialist economy (Roemer 1994c:296, 1991:565, Nove 1989:103). State-owned enterprises in Stalinism, in contrast to enterprises in market socialism, were under less pressure to adjust to changing economic conditions. In Stalinism, enterprises faced a soft budget constraint: If a state enterprise's spending exceeded its revenue, it received assistance to cover its debt, in the form of a subsidy, a reduction in taxes, an increase in credit, or an increase in the administered prices of the goods sold. In this way, the enterprise will always be bailed out in difficult situations.

For industrial democracy and self-management to be meaningful, the members of each state-owned, co-operative and even private enterprise will need to have a substantial degree of control over their work environment (Nove, 1987b, p.102). This will be reflected in areas such as decisions about the products to be made and the methods of production. Small co-operatives and private enterprises might want to decide most issues by general meetings. Larger ones will have probably adopted a more formal system of management, with top executives chosen by, and answerable to, the membership, but given a large degree of discretion in their day-to-day decision-making. It will be a mistake to regard time spent in decision-making as inherently unproductive. Workers' self-management at the enterprise level will be a

democratic process of decision-making and will foster and reinforce democracy at the political level. Workers will still require unions to protect them from overzealous managers, even if they have the power to remove management (Roemer 1991:567). Under market socialism, the national government will have no authority to hire and dismiss managers of corporations. Managers will be accountable to the rank-and-file employees through elections.

### **Inheritance Policy.**

Market socialists are very critical of the unfairness and inequity of capitalism, which is magnified by the fact that inheritance is clearly an important factor in determining the distribution of wealth (Yunker 1997:9-10). The resulting inequalities persist from generation to generation. In most capitalist economies, the majority of the rich are rich because they started from a privileged position (Estrin & Winter 1990:113, Yunker 199:44). This highlights the crucial importance of breaking the inequality cycle by drastically hindering the capacity of the wealthiest section of the population to pass on their accumulating fortunes through the generations (Estrin & Winter 1990:114; Roemer 1992:275). Under market socialism, the changing character of ownership and inheritance taxes will ensure equality of opportunity and the elimination of the unequal generational wealth distribution. Even if people have justly earned their estates, under conditions of equal opportunity, it does not follow that they have the right to exacerbate differential opportunity in the next generation by distributing their estates to favoured individuals. The requirement of equality of opportunity for the next generation is also a goal for market socialists.

### **Social Policy**

The goal associated with market socialism is greater equality at the beginning, so that people enter the market on an equal footing, to achieve the equalisation of positive freedoms in production (Estrin and Le Grand, 1990, pp.7-9). Indeed, raising the income of the poor will be the most important single step to improving their opportunities for self-realisation and greater welfare. To achieve this, households will require access to a guaranteed basic-liveable income without being forced to sell labour power to enterprises even though they are socially owned. The survival of the members of the society, at a basic but decent standard, will be independently guaranteed (Miller 1994:249-50). Under these circumstances, individuals will be able to exercise genuine choice about selling their labour power to enterprises, rather than being compelled to sell by necessity (Elson 1988:28). A transfer system based on the guaranteed basic-liveable income is not targeted at those who have shown to be 'inadequate'. It involves less administrative control over its beneficiaries and is far less likely to stigmatise, humiliate or shame them or undermine their self-respect.

A guarantee basic-liveable income for all citizens is linked with the classic market socialist concept of the social dividend as outlined by Oscar Lange (Blackburn 1991b:226) recently refined by Roemer and Yunker. It was that part of the national income which was not distributed as wages or interest but which belonged to the people as owners of the means of production. Profits of state enterprises will become a part of government revenue, which will fund the guaranteed basic-liveable income. An unconditional basic income will be a grant paid to every citizen, irrespective of his or her occupational situation and marital status, and without regard to his or her work

performance or availability for work. In this context, a taxes-drive-money or in other words a Chartalist approach to money will make sense. Based on the Chartalist approach to money, money is a creature of the state, as the state defines money that it will accept in payment for taxes. Because the public will normally wish to hold some extra money, under these conditions the government will normally have to spend or provide transfers (in our case guarantee basic-liveable income) more than it taxes. Hence the normal requirement for government is for a budget deficit, deficits will be accepted as the norm, consistent with Lerner's factional finance system (Wray 1998:18).

There will be a framework of objective minimum standards, which will be determined with the help of social scientists and approved after public debate, facilitating social solidarity and the promotion of social justice. The implementation of the guaranteed basic-liveable income will free the resources of the Department of Social Security, given that the taxation office will have administered the system. The Department of Social Security will be transformed and concentrate on the provision of services. The highly progressive tax system will ensure that those who did not require the guaranteed basic-liveable income returned the gain through the normal taxation process.

In line with this thinking, health, education and welfare services will be distributed according to need. Under conditions of full employment, the right-to-work for all citizens will be firmly established, without giving up the guaranteed basic-liveable income. Having these elements of social and taxation policies in place and with no private ownership in the means of production, there will be no private fortunes and no legal means of making money by speculation. Inequality will be reduced substantially.

### **Establishing a Market Socialist System.**

Market socialism will be established gradually, adopting firstly a minimalist approach and then move towards in time to maximalist approach. The first priority for a market socialist government that has been democratically elected, will be the establishment of the institutional structure to assist the development of the socialist market. Following a process will be initiated for the establishment of financial regulation, the tax structure and guaranteed basic-liveable income. The maintenance of private small firms and the transfer of medium firms to labour management will happen next. The restructuring of large state enterprises to self-management will also be initiated. Discretionary fiscal and monetary policy together with national economic planning and industry policies will be permanent features of the economic system. The right to work could only be implemented after the restructuring of state enterprises. At the end, socialism will be well embodied in the constitution with the requirement for a super-majority to reverse the socialist principles.

### **Conclusion**

In what way can the market socialist model proposed be called socialist? What is distinctive about the model that tries to establish a 'socialist' system? Ideologically, the model borrowed concepts and analysis from the liberal view, particularly the interventionist variant. It may even be argued that the model is contradictory. It tries to achieve a consistent socialist system through 'capitalist' means such as markets, prices, profits, market planning, 'bourgeois democracy' and self-interest. Strangely enough, the norms and institutions of capitalism appeared to be essential to socialism (Blackburn, 1991, p.ix; Howard and King, 1994, p.145).

Supporters of market socialism accept that capitalism has been able to sustain a high level of economic growth. Centrally-administered socialism was not able to match those levels. For socialism to have a chance, the economy has to adopt mechanisms that are not peculiarly 'capitalist'. Deng Xiaoping, the architect of economic reform in China, proclaimed that it does not matter whether the cat was red or white as long it caught mice. If market socialism does not discriminate against 'capitalist' mechanisms, what is left to distinguish a capitalist from a socialist economic system? Socialism stands, by definition, for humane rule and the subordination of economics to humanity. However, is market socialism simply "capitalism with a human face"?

Socialism, as envisaged by supporters of the model, is able to provide economic growth and, equally importantly, provide higher forms of accountability than capitalism. This is what is so special about socialism. It is no longer central administration replacing the market, or state property replacing private property, or even a single party system replacing 'bourgeois democracy'. These are not characteristics of socialism but, rather, of Stalinism, which does not have any relevance to socialism. For market socialists, socialism is described as a system superior to capitalism because it is able to eliminate some forms of power and, where power still exists, to control it more effectively than under capitalism. Although capitalism has achieved both high efficiency and accountability, socialism can go even further. The fact that non-pluralistic socialism failed to achieve these goals is an argument against Stalinism, not against socialism.

Although the market socialist model aims to reproduce the accountability of capitalism, it also envisages new forms of accountability. In particular, it incorporated national economic planning, beyond indicative

planning, and workers' self-management with election of management, which both have been inhibited under capitalism due to the power of domestic and international capital. One of the problems with a high concentration of private ownership in capitalist societies is its consequent influence on the political process. In the market socialist model, this is less likely to happen. Also less likely will be for the media to be influenced by particular interests. Therefore, it is argued that with the elimination of some and the effective control of the remaining centres of power, market socialism can achieve equality of opportunity for self-realisation, welfare, political influence and social status.

Hence the market socialist reforms will provide the basis for the development of a socialist ideology, which does not bear much resemblance to socialism as previously practised. Like all ideologies, it advocates the establishment of a superior form of society. It borrows methods and analysis from competing ideologies, particularly classical liberal and liberal interventionist concepts. The outcome will be different from all liberal as well as non-pluralistic forms. The model proposes a pluralistic society where the forms of ownership will facilitate a level of accountability beyond the grasp of a capitalist society. Such ideology is termed 'socialist interventionist', while the economic system is market socialism. While it bears a close resemblance to the liberal interventionist model, it attempts to transcend the levels of individualism and accountability achieved so far in capitalist societies.

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Union of Radical Political Economists  
[www.urpe.org/index.html](http://www.urpe.org/index.html)

Socialism Web Site:  
[home.vicnet.net.au/~dmcm/](http://home.vicnet.net.au/~dmcm/)

World Socialist Web Site: [www.wsws.org/](http://www.wsws.org/)  
Socialist International:  
[www.socialistinternational.org/](http://www.socialistinternational.org/)

### Introduction

The neoclassical mainstream model of the “market” has been successful over a century, in the sense, that it has largely shaped the general understanding of what a “market”, a “market economy”, and even an “economy” in general is, or should be. In its basic approach, it hardly has anything to do with the reality of markets, let alone with the full diversity of real economic forms. However, it has been made, through powerful forces, into an official economic thought system of capitalist-market economies and, thus, a *general theoretical and normative reference and benchmark* for economic analysis, economic systems and policies. This justification of the “market” has been achieved through the definition of a *decentralised economy* in which *prices* play a central role as coordinating devices, while this economy is defined as stable and being in an “optimal” equilibrium. While the “market” is an *ambiguous positive-normative ideal*, it nevertheless is considered not only an adequate reflection of the capitalist-market reality but also serves as a sound policy guideline for its reform. It is taken for granted by the great bulk of economists, politicians and the general public that this model of the “market” can, and should, be progressively approximated by state action.

To achieve this notion of the “market”, neoclassical economics has left unsolved the methodological question about the *realism and empirical relevance* of its basic model. Rather, it was suggested that, as long as its implications were applicable to make predictions and shape policies, reality could be supposed to behave *as if* it were consistent with the model, however unrealistic its assumptions (Friedman 1953:16ff). With this,

mainstream economics has always been a prime instance of a “paradigm” whose *theoretical core* is purely *axiomatic* and well protected against empirical counter-instances, and whose prime task is to give way to a “normal science” of endless model variations for a defined scientific community - and believing, or interested, political, economic, and mass media groups.

In the era of *neoliberalism*, the idea of a direct causal connection between neoclassical *modelling* and its normative *policy prescriptions* has indeed completely conquered the dominant system of norms and beliefs, and the legislation and measures of the leading political and administrative caste. Thus, neoclassical modelling has become a real-world force, a power that has shaped, and largely turned upside down, the structures of economy and society - “the embeddedness of the economy [plus society and politics–W.E.] in economics” (Callon 1998:23). (This is while “Neoliberalism” is neither “neo” nor can really be liberal, given its social “re-redistributive” ambitions, one-sided social interest commitment and, therefore, ultimately power-based and authoritarian character. This will be more elaborated below.)

The backside of losses of the neoliberal “model-reality-norms-policy” nexus has become obvious, though. The economy and society increasingly appear to suffer from *reduced problem-solving* and decreasing welfare-enhancing capacities. The *redistribution* of income, wealth, power and social recognition from the lower to the upper ranks, seems to have largely substituted a broader welfare enhancement and a more participatory development. Nevertheless, mainstream economists request, and politicians enforce, policies of “ever-more-of-the-same” kind. Thus, the “market” and “marsame” kind. Thus, the “market” and “market” economics increasingly seem to

have assumed a *religious character* (Nelson 2001).

An exact *definition* of an optimal, equilibrating and stable “market” economy is available only by referring to the highly abstract, largely implausible and even inconsistent, theory of the “*perfect market*” economy in a general equilibrium. The research programme of General Equilibrium Theory (GET), though, could never be completed to generate and consistently explain an “optimal” and stable general-equilibrium “market” economy.

Furthermore, the construction of the ideal model of a “market welfare optimum” is such that even the slightest deviation from one of its many restrictive axioms and assumptions may lead to *any* position in the solution space that may entail any welfare consequence, best or worst. There is no *second-best* definable then that the “market” would automatically achieve without state intervention. Notably, a real market has to be instituted and enforced, and market-oriented reforms have to be pursued, by its very *counter-principles*, i.e. social *institutions*, *hierarchies*, *networks*, and particularly the *state*. In neoclassical and neoliberal economics, however, the state is required both to minimise itself in favour of the “market” and be a strong de-regulator and protect the “market”. In this way, the neoclassical mainstream has always claimed some kind of natural independence and pre-existence of the “market”. It has even established the view that the state has to be considered like some private pure monopoly. Thus, the neoclassical and neo-liberal thrust is to privatise the state and reduce it to a minimum (Swedberg 1994:271ff; Daintith 1998:524ff; Chang 2000:21f).

*Coasian* Economics has justified this general thrust by referring *market failure* to the existence of *transaction costs*. So if a perfect “market” could be established by the definition of perfect private *property rights*,

public infrastructure and a related level of *information* and certainty, and thus all transaction costs be removed, all externalities could be internalised through private bargaining, resulting in an “efficient” resource allocation. The state’s agenda then would be to *privatise* all kinds of *commons* in order to reduce transaction costs (Daintith 1998:527f). However, as J.R. Commons (1934) already has established, the state, with its allocation of rights and duties, in fact also allocates a societal *power* distribution, thus determining the socio-economic *price structure* and *income distribution*.

We will focus in the following on the “*market*” model and its critique, its larger GET research programme, and its untenable *model-policy nexus* between “market” and state. If we consider, in contrast to the ideal “market”, *real worlds* of *directly-interdependent* agents, i.e. *socio-economies* proper, real markets come to be realised as something completely different than ideal “markets”. They turn out to be a part of the basic socio-economic problem, rather than its solution—if not properly embedded in a system of social institutions (Polanyi 1944).

We will have to ask then (1) whether an isolated *spontaneous decentralized* and price-led mechanism (a market) is really possible and probable, in a world of *directly-interdependent* agents, to be considered a *self-governing coordination* mechanism, (2) what kind of mechanism, or which *mixture of mechanisms*, is required for an effective coordination that gives way to real problem-solving, and (3) what the conceptions and roles of the *state* and the market, and their interrelation, will have to be in a more realistic view of the economy.

### “Perfect Market” as Universal Benchmark

The reference model in mainstream economics to prove the “optimality” and superiority of the “market” economy over any

other socio-economic form conceivable is the neoclassical model of the “perfect market”. Welfare economics states the (mutual) identity or implication of “perfect competitive market equilibrium” and the Pareto-Optimum (PO). However, it was demonstrated that if only one of the many highly specific and restrictive conditions of the PO was not met, it could not be determined. In addition, the model does not provide criteria or a measuring rod for gradual deviations. Thus, the “market” system could end up anywhere in the welfare space, even in the most disastrous position. The vague “neoliberal” idea that an ever closer realisation of “market-friendly” conditions (the welfare-economic “marginal conditions”) would gradually lead the real system closer to the ideal still seems to be intuitively plausible and even attractive. However, the *theorem of the second best* (Lipsey, Lancaster 1956/57) demonstrated that this assumption cannot be justified. And since there is no real-world equivalent, how ever vague, of a “perfect-market” economy, real-world “market” economies can be anything in the welfare space. Therefore, they can be either something workable or a worst possible scenario. Real markets, thus, have to be *evaluated concretely*, multi-dimensionally, in terms of real life and real human beings’ interests and aspirations rather than abstract price-quantity models.

In fact, the isolated *price-quantity world* in general is a heroic abstraction derived from a far more complex and substantially different real-world setting which displays many different price-quantity-interrelations if *changing “cetera”* are taken into account.

### Custom-Made Assumptions

The specific assumptions which prove the optimality of a “perfect-market” system are custom-made to establish a *mathematical procedure* that allows for *maximization* of

utility and profit functions under restrictions, and for a relation of demand and supply functions to yield, through “perfect” competition, the *equilibrium price vector* in an n-dimensional differential equation system.

On the *demand side*, the presupposition of some psychic mechanism of a marginal utility, i.e. the “law of demand”, with a decreasing marginal utility, is only vaguely justified through some rough plausible considerations. In fact, it has been custom-made to derive a demand function conveniently increasing in quantity with a decreasing price. Also, with the restricted substitutability of goods, a *convex* indifference function can be derived that allows for a maximum solution under a budget restriction (for a detailed critique, see Vickers 1996:3ff; Keen 2001:23ff). Furthermore, in the GET context, it can be formally demonstrated that a neoclassical general equilibrium requires all individuals to have *identical forms of utility functions*. The alleged individualist and liberal character of the “market” economy thus boils down to the implication of a grey uniformity - a system that does not allow for diversity but requests *isolated conformists* - individualism without real individuals.

On the *supply side* of the “market”, production and cost functions were elaborated from older plausible considerations about land as a bottleneck, i.e. *fixed factors* of (agrarian) production, *limited substitutability* among production factors and degressively increasing scale and marginal outputs, to meet the *convexity* and *increasing marginal cost* conditions in order to derive profit maxima and well-behaving supply functions (for more detail, see again Vickers 1996:8ff, Keen 2001:54ff).

Generally, in the price-quantity world agents are only *indirectly interdependent* since they are supposed to (re-)act only on

price movements, a result only of the totalities of the decisions of all other agents taken together on each market side. No price bargaining or other direct interactions are conceivable in this world, if the claim of optimality and superiority is to be maintained. This is due to the fact that exchange is conceivable, and in fact allowed, only at equilibrium prices.

### **Simplistic Micro-Macro Aggregation: The Invisible Hand**

The (partial) “perfect market” idea is supported by the idea of an invisible hand which suggests an *unproblematic aggregation* of individual decisions into aggregate demand and supply curves (the “economics of X”). Aggregation then is just a *static summation* of isolated optimisations, mutually harmonised through competition and equilibrium prices (where these prices also are supposed to meet the macroconditions of an identical system reproduction). Harmonisation is performed through an invisible hand in a way that the agents’ selfish aspirations are cut back and they *unintentionally* contribute to generate the welfare maximum, with no feelings of *frustration, envy, revenge* or *adaptive strategy* about their aspirations not being fulfilled. The “perfect-market” model thus allegedly is a formal representation of the pre-classical and classical invisible hand idea (Mandeville, Ferguson, Smith and others) and its laissez-faire implication. The classical idea, however, was used as a political metaphor and slogan against feudalism and mercantilism at that time. The neoclassical reconstruction, in contrast, was elaborated to meet *formal requirements* to prove the “optimality” of the “market” system (Ullmann-Margalit 1998:366ff), in fact a major *paradigm switch*.

The formal (partial) “perfect market” ignores, for instance, that *production* *uno actu* generates an income *distribution* and related

*consumption* and *price structures*. Even without considering more complex and realistic action-reaction chains, there is no guarantee that in the *circular flow* (i.e. in the GET frame) the resulting demand structure is compatible with the supply structure at any price vector that reasonably can be comprehended as generating some stable general equilibrium. In fact, as P. Sraffa (1960) has argued, every individual point on a supply curve (every different supply structure) entails a different structure of the utilisation of the factors of production, a different income distribution, consumption pattern and thus a different demand curve. Thus, there are *no given independent supply and demand curves*.

Also, the validity of the invisible hand as the *macrocondition* of the (partial) “perfect market” model requires modelling all societal spheres as perfect commodity “markets”. However, as K. Polanyi (1944) has pointed out, there are quite different conditions and behavioural schemes working in such basic and ubiquitous “markets” as land, labour, and money. These conditions, with their more complex action-reaction chains, prohibit simplistic neoclassical macromodels à la *Say’s Law*. The idea of a simplistic circular flow of expenses and incomes, however, still vaguely supports the invisible hand idea so that the average neoclassical economist may be easily confined to argue in the *partial* “perfect market” frame.

The recognition of *directly interdependent* worlds, direct-interaction chains and a more complex circular flow implies all kinds of *fallacies of aggregation* where aggregate outcomes may become highly idiosyncratic and may be far from “optimal”. In the real world and in more complex socio-economic models, aggregation of individual actions are problematic, based on path-dependent and open-ended interaction processes, subject to ongoing *conflicts of interest, circular*



*cumulative causations* and *sub-optimal coordination*. These consequences emerge as soon as direct interdependence, historical *time* and *diverse rationalities* and behavioural forms, and, thus, more complex micro-macro-interactions are considered (Vickers 1996:14ff, Shipman 1999).

### **Perfect Information**

In “perfect markets”, individual agents are supposed to be perfectly informed and to have a complete and “rational” preference ordering. In fact, the perfect information assumption has been largely put into question in economic theory, including even neoclassical approaches on information *asymmetries* and informational *transaction costs*. The transaction cost idea, however, has been neatly integrated into the “neoliberal” programme where the state has been made responsible to remove transaction cost obstacles to the “perfect market”. It is implied thus that “imperfect information” basically is exogenous to the “market” or at least has to, and can, be removed exogenously.

The “optimality” and superiority postulates of the “market” economy, though, can no longer be maintained with imperfect or incomplete information - such as *informational overshoot* and *bounded rationality*, objective *non-“knowability”* of future conditions and technological paths, *strong uncertainty*, including *strategic uncertainty*, and the *collective-good* and (interactively) *cumulative character* of information. Neoclassical “substitute” conceptions like risk and insurance market models (to generate “perfect knowledge” on future prices) are incapable of comprehending some of the most basic informational problems such as Arrow’s *information paradox* and *information indivisibilities*.

Much information, needed by individuals in the most basic coordination problems in a *directly-interdependent* and strategically

uncertain world, is a *collective good* where information has some value only if *shared* with others and will be generated only by cumulative interactive behaviour. Specifically, with *net-technologies*, as is the case with *social institutions*, the value of information often even increases with the number of people who share it (“net-externalities”). This is why the most basic social institutions are informational devices (again: parallel to informal technical standards) that can come into being only as *jointly learned* phenomena. Here agents have to recurrently interact and *cumulatively* contribute information through their decisions (Choudhury 1996:23ff).

Also *Austrian economics* considers information as a critical factor and Hayekian “markets” are conceptualised as evolutionary mechanisms. Austrians, though, maintain the superiority of the “market” system through the assumption that “markets” possess a sufficiently high information generating, diffusion and sharing capacity and, thus, coordination capability in order to allow an “optimal” system based on individual search and choice. However, it is highly questionable that predominantly price-based decentralized and competitive decisions alone have such an informational capacity, specifically to deal with fragmented and net-based decision-making and with ubiquitous information externalities, and to generate and diffuse such collective and cumulative information in a spontaneous and self-sustaining way (Shipman 1999:166ff).

In the case of non-perfect information, “perfectly” flexible prices will cause additional information costs through additional search, error and further price, cost and profit adaptations. The net gain of some new price information then may be well below the net gain from *fixed prices*. Fixed prices may then function as highly valuable information in uncertain and turbulent



markets. However, we are far from any “optimality” or “market” superiority under these conditions. “Fixed” situations, in general, may be important informational devices as, e.g., in oligopolistic markets, under conditions of economies of scale and zero-marginal costs, with resulting either ruinous price wars or price-agreements, or both.

With imperfect information, even complete *lock-ins*, i.e. some institutionalised, though “petrified”, “sclerotic”, and “old”, coordination, based on an outmoded, “non-optimal” technology, can well be *welfare-enhancing*, compared to a completely non-coordinated, dilemma-prone and turbulent “market” situation that easily may result in a complete *mutual blockage* of action (see below).

### Timelessness

In the “perfect market” economy, there is no room for *real (historical) time* and development, no irreversible and path-dependent processes as in real systems and in more complex socio-economic models. This is an implication of the minimalist structure of a *uniform representative agent* maximizing functions under restrictions and being only indirectly interdependent and coordinated through a price vector. This in turn was meant to solve the n-dimensional *differential equation system* that in turn was to represent the price-quantity world in a general “perfect markets” equilibrium and to formalise the invisible hand idea.

There is no *recurrent direct interaction* conceived which would give way to *process* and development, no space for *strategic action*, including *behavioural alternatives*, for search. Learning and adaptation.

In historical time, in contrast, a whole complex of conditions and factors, parameters and variables do change, such that systems become *path-dependent*, i.e.

the way they have taken and the positions assumed earlier are crucial for the current condition and further perspectives of the system. Complex evolutionary systems also are *non-ergodic* and *irreversible* in that a current state of the system is not fully determining future states (while “market” economics with perfect information implies complete mechanical reversibility and ergodicity; Arestis 1996).

In the real world of *functionally and spatially fragmented global production and innovation chains*, with net-technologies as their technological base, where highly integrated and complex products are produced, any individual decision has an immediate and considerable informational impact on others, i.e. production and innovation are systems of *informational externalities* or *spillovers*. Thus, information needs to be managed commonly and shared in order to avoid lock-in or mutual blockage of action in “markets” with isolated “rationally” maximizing agents (market coordination failure). Agents then have to develop a collective action capacity to escape mutual blockage or a renewed collective action capacity to escape a lock-in. Lock-ins, in fact, can be viewed as a rather usual path of spontaneous decentralised systems under the condition of direct interdependence and strong (strategic) uncertainty when sufficient coordination is lacking and a continuing or renewed collective action capability is not sufficiently developed (Callon 1998:48ff, Elsner 2006).

Neoclassical economics deals with all kinds of variations from their core model nowadays. But these variations are not apt to support the theoretical and ideological main thrust of neoclassical economics, i.e. that a general market economy is “optimal”, equilibrating and stable, and superior to any other coordination form. Variations are applied to all kinds of *partial equilibrium*

models but typically cannot be applied to elaborate on the model of the “market economy” as a system, i.e. the GET frame. In fact, the neoclassical attempt at formalising the invisible hand was unsuccessful.

### **Non-Feasible General Equilibrium Research Programme**

The GET has always been considered the top tier of economic theory, the completion of the neoclassical research programme and the proper proof of the superiority of a “market economy”. This research programme in fact could not be completed. In an Arrow-Debreu world, the *existence* of “an” equilibrium can be proved. However, the ideal general “market economy” turned out to provide too little structure with its isolated uniform utility and production functions in order to exclude at least some of the infinite number of potential equilibria. In fact, no unique equilibrium can be defined.

The programme failed even more with the establishment of an adaptation mechanism, i.e. the *stability* of such equilibrium. The latter could be indicated only through the utilisation of inconsistent mathematical elements, taken from inadequate physical analogies, entailing some economically senseless implications such as perfect *reversibility* and energy conservation. Specifically, Samuelson’s *Foundations* (1948), considered “the” neoclassical foundation of the “market economy”, represent an inconsistent compilation of selected physical metaphors [such as the timeless field theory of the value vs. the theory of dynamic (differential equation) systems which uses time], in this way largely assuming rather than proving the stability of the GE (Wellhoener 2002). In fact, the *Sonnenschein Theorem* (Sonnenschein 1972) proved that a neoclassical “market” system generally does not possess a stable equilibrium (Mirowski 1989).

The GET also has *institutional* and philosophical *implications* that contrast its own ideological postulate and social message. Walras’ *tâtonnement* idea implies an *auctioneer* with the power to prevent people to trade at non-equilibrium prices. If equilibrium prices are determined, however, trading is meaningless, and exchange is an anonymous, quasi-centralized automatism. Suppliers might equally bring goods and money to a central store and demanders get their goods and revenues allocated from this stock, or central computer, in complete anonymity, an absurd vision of transaction and exchange. The liberal individualist(ic) message of the “market economy” turns into a highly *centralized, authoritarian* system with a quasi-dictator. “Optimality”, equilibrium, and “individual freedom” seem attainable only with *anti-individualist* and *anti-liberal* methods.

*Non-tâtonnement* approaches have been developed in the frame of the neoclassical research programme, however. They allow for exchange at “wrong” prices, at the expense of further inconsistency, though, among axioms and formal methods used (s. Wellhoener 2002:212ff). Their equilibrium, stability and welfare implications have become more ambiguous, rather than supporting the neoclassical desiderata of optimality and superiority of the “market” economy.

In addition, a (capitalist) “market” economy can, by its very character, never be a closed system, self-equilibrating and self-sustaining, but is an *open system*, as has been elaborated in the traditions of K.W. Kapp, N. Georgescu-Roegen and others. An open system systematically utilises and generates externalities vis-à-vis the natural and societal environments (Callon 1998:244ff). Capitalist “market” economies have a particularly intense *metabolism*, absorbing “structured” energy of a low *entropy* from the other two

sub-systems, natural and social, in order to accumulate individual pecuniary value-added, in this way by-producing “unstructured”, “dead” material of low energy and high entropy in large quantities (Lutz 1996:115ff).

### **Complexity, Uncertainty, and Power**

Among the assumptions of mainstream economics are homogeneous rather than diversified or branded goods, costless entry, zero sunk costs, no economies of scale or indivisibilities, no oligopolies, collusions or power. However, *indivisibilities* and *collectivities*, *inappropriability*, externalities and *dilemma-prone* coordination problems are much more pervasive in the reality of the “*new economy*” than can be reflected by neoclassical economics. In fact, they have become ubiquitous in production and innovation processes (Callon 1998:16ff; Elsner 2005). For instance, *non-substitutable* factors of production have implications for income distribution and the whole circular flow of supply and demand (Keen 2001:85ff, 110ff).

Specifically, with digital microelectronic technologies there appear *near-to-zero marginal costs* of an increasing number of products. High fixed costs, often including strategic *sunk costs*, and intense *economies of scale*, including considerable learning economies, undermine well-behaving supply curves and “market equilibria” and involve processes towards *oligopolistic* and *monopolistic* structures (“natural” monopolies). The historically unprecedented global sales share of some 85% that Microsoft’s operating systems have obtained would be incomprehensible without giant economies of scale and the cumulative *net-externalities* implied in the “internet economy”.

*Entry* into the leading oligopolistic spheres of the markets is largely prohibited for the normal business founder nowadays. He may

find niches, end up as a highly controlled supplier for the oligopolistic brand assemblers, or will be bought up by them in the end. Most markets are established oligopolistic *power* structures, with tendencies towards either ruinous fights and/or pre-emptive collusion at the expense of third parties (including small and medium-sized potential entrants, the state, and the general public). In the fragmented “new economy”, power and *hierarchy* also combine with *network* structures. Thus, corporations control not only huge vertical “in-house” hierarchies but also global hierarchical *hub&spoke* networks with thousands of first, second and third tier suppliers and hundred thousands of labour force.

More *de-regulated neoliberal “markets”* are subject to even stronger uncertainty, *turbulence* and *turmoil* (Burlamaqui 2000:44f). The spontaneous individualist(ic) reactions of powerful agents to this is to gain ever *more power* in order not to lose *control over their environment*. Hierarchy and power are the normal ways agents in de-regulated markets try to reduce complexity and uncertainty. And the more power comes to be the dominant allocation mechanism the more the system works *re-re-distributively* rather than through welfare-enhancement. Powerful agents, in turn, ask for more de-regulation, and so on.

The *natural individual*, as a consumer, self-employed entrepreneur, or citizen, is confronted in this way with ever larger and more powerful *corporate hierarchies*. Neoclassical economics, however, has never addressed this basically *unequal power relation* between “individual agents”. Behind the veil of “equal agents”, however, the pseudo-person of the corporate firm has been supported and sheltered by mainstream economics, and legislation and jurisdiction as well, with every right to pursue its maximum

profit as a publicly protected “common good” (Lutz 1996:116f).

There is a long tradition in political economy and evolutionary-institutional economics to analyse the implications of (de-regulated) corporate power. *Absentee ownership*, “*pecuniary*” *sabotage* of industrial production by financial investors, productive restriction, re-distribution, and intervention in the political process, *ceremonial* expenses and the enforcement of the ceremonial dimension of the social institutions have been major issues in the Veblenian, Berle-Means and Galbraithian traditions (Lowry 1994). Phenomena of *non-productive corporate behaviour* include service deterioration, *short-termism*, “financial-ism” and *stakeholderism*, quality shaving, cream skimming, standards undercutting etc. (Lutz 1996, Nelson 2001:3ff), increasing indications of Veblen’s idea of sabotage of industry.

Power imbalance also is reflected in such diverse phenomena as *elasticities* of supply and demand, *information asymmetry*, *incomplete labour contracts* etc. (Bowles, Gintis 1999; Shipman 1999:263ff, 359ff; Keen 2001:85ff). As has been put forward by classical, Marxian and Schumpeterian political economists as well as institutionalists of different traditions, the “market” inherently tends to *undermine itself* (as an embedded and aptly competitive, i.e. problem-solving mechanism) through the very principles of hierarchy and power (Callon 1998:46ff; Abolafia 1998:76ff). The irony and inner contradiction of de-regulated markets is that the most powerful corporate forces in turn establish *centralized private command economies*, and that, in turn, the state is forced to establish an authoritarian regulation to keep control over other societal areas, interests and groups and a disintegrating society in general (Munkirs 1985; O’Neill 1998).

This mechanism, rooted in basic contradictions between neoclassical “market”-conceptions and reality, contrasts neoliberal promises of increasing personal liberty. Thatcherism, Reaganism, Bushism and Blairism seem to be instances for “reforms” to entail decreased problem-solving, increased economic mal-performance, even potential anarchy, and subsequently increasing authoritarian reactions (Toruno 1997; Briggs 1998).

The ubiquity of direct interdependencies and the reactions of private agents to de-regulation and privatisation, in terms of hierarchy, power, collusion and hub&spoke networking, reflect the increasing *degree of socialisation* of all production, innovation and consumption, as such diverse economists like Marx and Schumpeter have elaborated (Burlamaqui 2000).

### **Social Institutions, Embeddedness and Dis-Embedding of “Markets”**

Any *good* or service, in fact, is part of a socially *embedded interaction*, i.e. has a dimension beyond its physical exchange. In every transaction, *coordinating social institutions* have to be established or confirmed, corresponding expectations and *trust* be generated, reproduced, or further developed (De Jasay 1998). With “rational”, individualistic, short-run maximising behaviour alone, however, institutions would be questioned, undermined, broken and deteriorated, or even their emergence prevented.

With *direct interdependence*, every agent is facing more than one *behavioural option* at any one time. There is always the opportunity, and in markets even a *dominant incentive* (if not ruled out by institutions or formal systems of control and sanction), to exploit a trusting interaction partner, i.e. to assume a *free rider* position. Nevertheless, real-world markets are institutionally

*embedded* systems, however weakly embedded, otherwise they would not have come into functioning at all. They can be comprehended only, and also can work only as mechanisms with a role for supply, demand and prices, as embedded in a system of societal institutions that provide sense and meaning to any individual action (Neale 1994; MacEwan 2000:chpt. 4).

Social *institutions* do not primarily define “limits of the market” but are at the core of *problem-solving*, *enabler* of effective coordinated action capability, *freeing* the individuals from strong uncertainty, mutually blocked action, and suppression by powerful other agents - in this way remaining to be limits to the “market”. They reduce *opportunism*, stabilise expectations by providing information about expected behaviour, and reduce transaction costs, in fact part of the *instrumental* dimension of institutions (Swedberg 1994, Choudhury 1996). International surveys (even conducted by the World Bank) provide ample material on the correlation between the levels of *trust*, conveyed by institutions, and overall economic *performance*.

Institutions include informational economies of scale and positive *cumulative* effects, “net-externalities” and spillovers in a wide sense, in that their value increases with the number of users and the frequency of their use. Also “markets” are results of myriads of social interactions, and prices are socially established values, rather than “natural” givens (Clark 1993; Abolafia 1998).

There is no allegation, though, that institutions solve a problem once for all. Institutions are *past-bound* condensed social experience and information. They provide *stability* through coordination (and on this basis even giving opportunity for *innovative action*) rather than being immediately future-bound. In addition, the Veblenian institutional dichotomy indicates that institutions, besides

their problem-solving capacity, may adopt, in power-based and hierarchical contexts, a major *ceremonial* dimension by which differential power and status are perpetuated.

Against this background, “markets” can not be generally *defined*. There is hardly any general definition feasible or a common set of properties determinable beyond the fact that there are in some way decentred suppliers and demanders and that prices play “some” major role. Beyond this, “markets” can be anything, depending on their institutional embedding. They result from their institutional *framing* (Callon 1998:16ff,42ff). Accordingly, “markets” are consistent with a huge variety of societal ends, means and *rationalities*, and even modes of calculation (Swedberg 1994:255ff, Abolafia 1998:69ff, Zafirovski & Levine 1999).

“Markets” have regularly been established and protected through (often violent) *enforcement by the state*. Typically, it is the state that defines economic agents, property, commodities to be exchangeable, rules and boundaries of “market”-related activity etc. “Markets” were historically developed by state and military bureaucracies in the context of re-distributions and often ceremonial exertion of rights, duties, information, power and physical resources (Clark 1993, Neale 1994, Lowry 1994:47ff, Callon 1998:40ff).

Dis-embedded neoliberal “markets”, in contrast, tend to *dominate the societal/cultural system* as Polanyi, Kapp and others have elaborated. In this way, the problem-solving capacity of a society decreases and *social costs* and crises increase (O’Hara 2000:183ff; Elsner 2006). The de-regulated “market”, with its increasing tendency towards *opportunistic* behaviour, tends to consume and deteriorate social institutions. In doing so it tends to replace the welfare-enhancing capacities of a society through a rampant *ceremonial dimension* (Toruno 1997).

Also, de-regulation has enforced an exaggerated and counterproductively fierce “competition” and in this way increased the *vulnerability* of economy, natural environment and society (Lutz 1996, O’Hara 2000:253ff).

### “New” Economy, Complexity and Social Dilemmas

As has been indicated, in the “new” economy, agents are increasingly facing ubiquitous complex decision problems with considerable coordination problems, often dominating (latent) *incentives to defect*, and (latent) mutual blockages or lock-ins. Huge international bureaucracies, both state and corporate, therefore, care for *technological standardisation*, interfaces, protocols etc. to limit these latent problems and to make technology *supportive of behavioural standardisation and coordination*. Such hierarchical solutions are the other side of the coin of disembedded markets.

Obviously, the “new” economy must be organised as a system of *complementarities*. Even some re-embedding in *regional clusters and networks* has become a way of global corporate players to gain control over their environmental conditions and to improve the performance of their most important corporate divisions through *proximity, recurrence, stable interrelations, commitment* and some cultural embeddedness (how much interwoven with power and hierarchy ever) – all of this being in contrast to the neoliberal “market” rhetoric. This is a strong indication of the fact that an individual agent is directly interdependent with others and any individual action is *strategic interaction*. This regularly defines a *dilemma-prone* social decision space.

### Evolutionary Solution

In directly-interdependent decision problems with a collective-good dimension involved,

agents, in a first or one-shot encounter, are confronted with different behavioural options and thus, basically, *initial strong (strategic) uncertainty*. The “invisible hand” then tends to generate a social bad rather than a good. Notably, *ubiquitous opportunistic behaviour* may be welcome in a neoclassical view where cooperation is comprehended as collusion against third parties (competitors, consumers) only, since the environment otherwise allegedly is perfectly competitive.

Under the condition of initial true strategic uncertainty, however, non-opportunistic behaviour, namely *cooperation*, is required as a form of coordination and joint management of collectivities and spillovers where the individualist short-run extra profit is *sacrificed* in favour of some *long-run* optimisation over both the *private* and the *common goods* dimensions involved. The economy has to be modelled then as a genuinely multi-personal or *societal* situation. This renders the economy a complex system in terms of a potential multiplicity of relations among each two agents. In *recurrent* interactions agents then may learn, in an *evolutionary* process, to develop *institutionalised* forms of social coordination. Evolutionary models may then demonstrate the generation of *self-sustaining* aggregate structures, i.e. stable behavioural patterns (Choudhury 1996:23ff; Ullmann-Margalit 1998:368ff).

### Spontaneous Order and Self-Governance

Real-world social dilemmas are complex because of *multiple relations* among each two agents. This can be illustrated by a simple *Prisoners’ Dilemma* (PD) structure with two agents, two pure strategies, a cooperative one, C, and a defective one, NC, and a simple payoff space:

	C	
C	b, d	c, c
NC		

with  $b > a > c > d$ .

As has been said, every single decision in a real-world economy has to contribute to some *collective framework good*, i.e. the (re)production of the “environment” of social rules and behavioural expectations. The PD structure reflects this very fact, i.e. that any transaction includes a collective good dimension.

*Effective action* becomes feasible here only by way of *complexity reduction*. The conventional and spontaneous device to reduce complexity in market economies, again, is to resort to hierarchy, power, and hub&spoke structures. With social dilemmas, the reduction of complexity requires decreasing the number of multiple relations and a *power-free*, decentralised, *informal* and self-governing complexity-reduction device here is collectively learned institutions. This may lead, under certain conditions, to institutionalised mutual cooperation (or reciprocity) in the face of major individualistic incentives to defect. This in turn requires *recurrent* interaction and the development of mutually consistent expectations, i.e. *time*, process, and *futurity*.

The coordinated behaviour then *habitually* excludes or restricts short-run maximization. People then do not behave too “rational” or clever anymore. The reconciliation of the “mixed-typed” (partly competitive, partly consistent) individual incentives in a PD is only conceivable as a commonly accepted habitual rule, i.e. an *institution of cooperation* where “rational” opportunism in fact is “ruled out”. Complexity, then, may be reduced to a level where individuals can reasonably be expected to act effectively, that is to manage the then *reduced level of uncertainty*. In this way they become *capable to act* and even *inclined to innovate*, i.e. to develop more comprehensive problem-solving through

future-bound behaviour. In the face of a level of turbulence which is too high, the individual, and also the small and medium-sized enterprise, indeed, are incapable of being innovative in a reasonably comprehensive, deliberate and sustainable way.

A more formal illustration is conceptualised here in a social setting characterized by direct interdependence and a social dilemma of the PD type, i.e. an individualistic culture at the outset. This can be taken as a *worst-case* view of a setting in which institutions of coordination are not dominant yet. Furthermore, recurrent interactions are assumed, i.e. infinitely or indefinitely repeated interactions (a PD *supergame*) between the same players. If more than two players form the *population*, the same pair of players will meet with some definite positive probability  $0 < \delta < 1$ . Finally, we assume some *sequentiality* of decision-making, i.e. giving room for *processes* of institutionalisation. This implies that individuals may *change their strategies* in the sequence of interactions.

As is well known, coordination failure is demonstrated in a *one-shot* PD or a PD with a finite and known number of rounds. The *collective good* is inaccessible then to the agents. However, if we define a *private good* as a good that can self-sustainingly be produced in the process of interaction of private agents, then the *transition* from a one- or finite-round PD to a supergame may imply the transition from the collective to a “private” good.

A simple *single-shot* solution of that PD-supergame is the following.  $\delta$  also serves as a common discount parameter. A cooperative agent interacting with another cooperative one gains the payoff for C, i.e. PC:

$$PC_{(C,C)} = a + \delta a + \delta^2 a + \dots = a/(1-\delta) \quad (1)$$

A cooperator has to be specified here, however, not as an ALL C player but one who always begins cooperating and then plays what the other one played the round before, i.e. the well-known TIT FOR TAT (TFT) or TRIGGER strategy player.

While one player plays TFT, a defecting player (playing ALL NC) gains PNC:

$$PNC_{(NC,TFT)} = b + \delta c + \delta^2 c + \dots = c/(1-\delta) + b - c. \quad (2)$$

Cooperation then pays if

$$\begin{aligned} PC_{(TFT,TFT)} &> PNC_{(NC,TFT)}, \\ \text{or} \\ \delta &> (b - a) / (b - c) \end{aligned} \quad (3)$$

The superiority of cooperation depends here on the relative pay-offs  $a$ ,  $b$  and  $c$ , i.e. the *incentive structure*, and the discount parameter  $\delta$ , i.e. the *futurity*. Particularly, cooperation will be feasible when the future plays a sufficiently large role in relation to a given incentive structure. The *long-run perspective* thus is a precondition for coordination success, i.e. self-organisation. This is the famous *folk-theorem*.

However, this result is just a logical one based on a *static* approach with fixed strategies in which only a single decision is made by the agents. In contrast, we have assumed a process of sequential decisions with interactive learning, i.e. *change of strategies*. Thus, we have to show how cooperation emerges through joint learning among agents who defect in a one-shot game. Regarding this, we will only roughly refer to the literature here.

In a population with a given *initial distribution of fixed strategies*, the superiority and *evolutionary stability* of cooperation, in an evolutionary process, depends on the portions in which the different strategies are represented. Individual interactive learning may be formally represented by a *replicator* mechanism. This determines how the

numbers of individuals in the *sub-populations*, representing certain strategies and scoring in certain portions in the recurrent encounters with each other, change from one round to the next, i.e. gaining or losing members, or having more or less offspring, according to their relative pay-off success. This mechanism may be viewed as simulating individual *learning*, i.e. individuals changing their strategy adherence and sub-population. The object of selection and reproduction here is, of course, considered the type of behavioural rule (the institution or culture of the sub-population), not the physical agent.

Axelrod (1984), as is well-known, employed a replicator mechanism in a population initially consisting of equal portions of more than 60 different strategies. He demonstrated the *emergence of the institution* of cooperation and the evolutionary stability of the most simple cooperation strategy, TFT. He also demonstrated that cooperative strategies may survive and even diffuse starting from only rather small portions in the total population, i.e. in a relatively hostile environment (not because they gain against defectors but because they are so successful with each other). A conception of cultural evolution, however, will require a more explicit conception of individual *search and learning* mechanisms. There are many approaches and models to formalize cultural-evolutionary processes which employ algorithms of “crossing” and “mutation”, i.e. search, experimentation, and adaptation through learning (from one’s own experience, through imitation), e.g. from a common frustration of two defectors. They show that cultural evolution in PD-settings indeed may result in the emergence of institutions of cooperation (Schotter 1981; Liebrand, Messick (Eds.) 1996; Kirman 1998).



These results sometimes have been falsely interpreted to *support neoliberal postulates* of the “efficiency” of the “market” economy, now comprehended as evolutionary. Solving a PD supergame through cooperation definitely is *not a neoclassical “perfect market” solution* since coordination is not gained through prices based on isolated short-run maximisation under perfect information and competition. On the contrary, the solution is gained by some form of interactively learned, collective, and institutionalised coordination, having emerged independent of, and prior to, any “market” coordination. Although agents are seen here to strive for maximisation in some way, they have to be “irrational” in some aspect in order to overcome the dilemma and learn to cooperate in a sequential process. For instance, the first to offer cooperation will have to be “risk-friendly” and *non-envious* since the least he has to expect is to be exploited once by the other before the other one possibly also changes to cooperation.

Calculating the single-shot supergame payoffs for TFT/TFT, NC/TFT, TFT/NC and NC/NC may yield the so-called *assurance game* or *stag hunt* payoff matrix which displays the different potential “condensed histories” of the supergame. An ALL NC player playing against a TFT player may well get off then with less than a TFT player playing with another one, with normal specifications of the payoffs and the discount parameter. So this new matrix may have *two Nash equilibria*. A. Sen developed the idea that, as far as a player can be “assured” that the other one will cooperate, the Pareto superior situation may become the “natural state” (Sen 1967). However, the suggestion of a *Rousseauian “social contract”* as a general frame of “assurance”, in fact, refers back, in an infinite regress, to the evolutionary process of joint learning of institutions, the emergence of a “social contract” in this case.

Institutional emergence, from a “worst case” starting point of short-run maximisers, will have to add more elements to the static formal solution, such as emerging *search* on the background of *repeated frustration* from common defection, combined perhaps with some not too great length of memory (to be able to forget bad experience), etc. (De Jasay 1998:96).

However, the overall argument seems to be supportive of our argument that the process of emergence of institutions of cooperation is *not per se self-sustaining*. In fact, the basic social *dilemma* would always *continue to exist* in the background. This is reflected by the fact that the spontaneous evolutionary emergence may be highly *time-consuming* and *fragile*. And the more individualistic a culture is, that is, the stronger the dilemma-structure in terms of the specific numerical relations among  $a$ ,  $b$ ,  $c$  and  $\delta$ , the greater the incentive will be to defect. Also, the incentive to defect will increase for a “rational” or clever defector as soon as an institution has been established and he can expect the others to habitually cooperate. Simulations, accordingly, have illustrated that cooperation may be unstable and occasionally collapse because of internal dynamics (Lindgren 1997).

Moreover, in a *dynamic* environment, collective action even is required to transcend a coordination already achieved, when conditions have changed. Institutionalised coordination, thus, has to be conceptualised as dynamic as well, i.e. *continuing collective action capacity* to change institutions in order to *reflect change*, avoid lock-in, and make traverses towards new paths with a new societal knowledge fund and technology feasible. This would differ from a “neoliberal” conception of “flexibility”. There is a *flexibility/turbulence* vs *stability/coordination trade-off*, and viable economic conceptions have to be more balanced than

isolated neoliberal “flexibility” postulates that in fact ever more generalise market failure.

However, this cannot reliably be achieved in a setting with private agents only. An agent with *another logic* of action must be introduced, to reduce the system’s idiosyncrasy and contribute to a greater system resilience. This is confirmed by many evolutionary approaches to coordination and *state formation* (De Jasay 1998:98ff).

Particularly, the *collective good* that even a perfectly working network, based on well-institutionalised cooperation, generates typically is not confined to the *limits of the network* or “club” that generates it. It normally is *functionally, personally and/or spatially more far-reaching* than the boundaries of the private network. There are *spillovers* and room for “free-riders” outside the generating network. Even if the cooperating “doves” may feed a certain portion of “hawks” and be even better off than with a general default, this is a case for state activity to stabilise the coordination and collective production of the superior good. It seems necessary, therefore, to introduce a more *supra-individualistic rationality* into spontaneous, decentralized, evolutionary processes among private agents. *Public-policy* frame-setting is required here, if not to completely initiate (i.e. de-block, un-lock), to *accelerate* and *stabilize* processes of institutionalisation of cooperation which cannot be brought forth with sufficient certainty, speed and stability by individualistic rationality alone. This is also what the game-theoretic argument comes to conclude.

### **State in Interdependent and Evolving Decentralised Economies**

Thus, both empirical evidence and theoretical consideration suggest a *new role of the state* vis-à-vis the market, i.e. the interaction processes of the private agents. The state then

has to deal with *shaping and stabilizing* the joint learning of coordination and the *conditions of interaction* in general. To this purpose, there is a “strong” state required to *define the public good* and objective and to (de)meritorise the private interaction result. The state has to be legitimate, strong and committed enough for a *stable long-term framing strategy* (Burlamaqui 2000:40ff).

In mainstream economics, the *collective-good* problem has been regarded as a *purely public* task. However, neoclassical *Public Choice* theory, meant to cover those collective and directly-interactive areas that the otherwise “perfect market” leaves aside (through discourse and coalition building), faces the same individualistic problems of coordination that are faced by the “market’s” individualistic dilemmas. (This also applies to some branches of the so-called *cooperative game theory* that have to refer to more or less external sources of enforcement.) This view also has unduly shifted responsibility away from the *private agents* who, in pursuing their own individual interests, are facing considerable *incentives to contribute* in order to solve the problem, as the simple PD incentive structure illustrates. Private agents have a definite interest in the production of the collective good, regardless of the fact that it cannot be adequately produced by them because of coordination failure inherent in their spontaneous interactions. The public agent, consequently, can request the private agents to contribute. This allows for a *leaner policy* approach.

A related insight from the PD-structure is that the collective good problem can be seen as a *gradual* problem. If the public agent would sufficiently subsidize cooperative behaviour he could dissolve the dilemma structure as such. But this might entail high subsidies. Problem-solving, in contrast, can already be promoted by *gradually weakening the dilemma structure*. In a numerical

example, say  $\delta = 0.9$ ,  $b = 4$  and  $c = 2$ , equation (3) implies that cooperation would already be superior to defection with a value of  $a = 2.2$ , i.e. already with limited incentives, cooperation may come into existence with increased probability, speed and stability.

The reason why a leaner policy becomes possible is that the approach allows for a *clearer definition of the relative interests*, or benefits, as well as a clearer allocation of the relative responsibilities, or costs, *of the private and public agents* - as opposed to fuzzy “public-private partnerships” that are in fashion. Also, it allows for *process* and related *learning investment* of the private agents rather than static preference-based decisions.

The (potential) outcome of the private interaction process, though, has a public value in addition to its private values and thus can be related to a policy objective in such a way that it can be made subject to (de-) *meritorisation*. The conception of the *merit good* implies a social evaluation of the outcome of the market through some kind of social decision-making which is more comprehensive than, *independent of, prior and superior to the market* (Brennan, Lomasky 1982; Musgrave 1987; Ver Eecke 1998). Obviously, a more comprehensive *political economy* is required which includes *deliberative* and *discursive* mechanisms of interaction in order to yield public collective decision-making capacity vis-à-vis the private economic interaction processes.

For instance, the conception of the *negotiated economy* has been elaborated in institutional economics to understand that and how the market has to be deliberately embedded in a wider socio-political process (Commons 1934:612ff, 649ff; Nielsen 1992; Shipman 1999:214ff, 439ff). In this process, public policy objectives can be independently developed which provide the criteria for the “meritorisation” required.

Against the background of the above, we can define now a *merit good* as something which is a *collective good* at the outset, but can, in principle, be produced by the spontaneous private interaction process described, i.e. a *private good* as defined above. The good is meritorised then mainly regarding the *time span* needed for its production as well as the *stability of its provision* through private interaction.

The first complex of *instruments* then aims at changing the *incentives* in order to increase the relative rewards for cooperation or decrease the opportunity costs of cooperation. Notably, the incentives for cooperation may largely consist of *non-pecuniary* benefits (Klein 1990; Elsner 2001:76ff). Equation (3) also shows that the more successful the public agent is in involving the private agents into a future-bound process, i.e. the higher the discount parameter  $\delta$ , the less the increase of the incentives needs to be.

Since the  $\delta$  can be interpreted not only as the weight allocated to a future pay-off but also as the probability of a future interaction among the agents, the second complex of instruments, refers to the *futurity*, i.e. the probability of private agents to meet again in the future. Cooperation can be promoted if future interactions become more probable. This will typically be the case in “*medium-sized*” *groups and platforms* as this probability decreases with an increasing group size. In this way, local and *regional clusters* and *networks* are confirmed as being important objects of such a “*meso*” *policy* (Elsner 2000). Among the success factors of cooperation, thus, are small group size, “proximity”, and the frequency of interaction (“density”), but also some reputation mechanism which increases  $\delta$  again if it has declined in growing groups (Hirschleifer 1998).

This condition can indeed be made subject to policy control. As Axelrod (1984) has

already pointed out, the public agent can increase the probability of future interaction. He can make cooperation more permanent through more frequent meetings, by dividing projects into several sub-interactions, connecting different projects so that the same agents will meet in different arenas and become more aware of their common future, etc.

In sum, this *institutional policy* approach and state conception may help to change the behaviour and expectations of the private agents by changing the pay-off structure and time horizon of their interactions. Thus, it *interacts* in a specific way with the interaction process of the private agents (for the basics of “institutional” economic policy, Tool 1979; Hayden 1994, 2006). This approach has already been elaborated into operational policy conceptions which form a broader, non-mainstream, and *post-neo-liberal approach to governance and the state* (Jessop 1994, Block 2000, Chang 2000, Burlamaqui 2000, Yu 2000, O’Hara 2000:266ff, Elsner 2001,2005). Thus, the *market* can be analysed in a new way and be put in a new and *more consistent and sustainable relation to the state*. The approach also offers ample opportunity for further research to establish a more relevant approach to the “market-state” interrelation on an evolutionary-institutional basis.

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## Monarchism and Republicanism

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### **Introduction**

Monarchist ideology defends a state that is based on the authority of one person with exclusive right to the office of chief of state. Its most direct alternative is republicanism, which defends the abolition or absence of a particular discriminatory state institution. Republic is a word coming from the Latin “res publica”, “public thing” or “common wealth”, and stresses the idea of the commonality of public goods and an egalitarian, non-discriminatory way of exerting authority in the state. Nevertheless, the dichotomy is not always sharp. A notional monarchy may really be linked to dominant republic if we consider republic synonymous of a democratically system of government. But, as we shall see, republic and democracy have not historically been considered perfect synonymous.

Kingdoms, empires and principalities are different types of monarchies. Today, the kingdom, where the office of head of state is by law reserved for the members of a family or families, is the most common type. So, the highest office is not open to all but bestowed on biological-materialist relationship of blood or parental relationships rather than on personal capacity or merit. Kingdoms are normally also based on a sexist principle, as the first son will succeed the monarch even if he has an older sister; and on marriage, as a male offspring of the king conceived out of marriage is not supposed to have succession rights. In some cases, it is also based on religion, as is the case with the British Kingdom, where the Head of the State is also the Head of the Church.

Economic institutions are said to be a consequence of political institutions. With a rent-seeking methodology, Ekelund and

Tollison (1997) concluded that mercantilism was a result of absolute monarchy, introduced by Henry VIII. Parliament ended this in the seventeenth century British “glorious revolution”, and rent seeking was made more difficult, as separation of powers increased the cost of supplying and demanding regulations.

### **Antecedents of the Dichotomy**

Although Plato’s great work has been translated Republic, as stated in Forsyth and Keens-Soper (1988) in Greek it was called Politeia, for which “regime” may be a less misleading translation. It is true that the Greek poleis from around 550 BC were significantly different from the monarchies and aristocracies from which they had evolved: rulers no longer treated subjects almost as property and people felt loyalty to the whole polis rather than merely to a clan or tribe. But at first the classification of political constitutions did not present the monarchism/republicanism dichotomy. For Plato, the ideal city is one ruled by lovers of wisdom. That meant aristocracy, the rule of the best. Aristocracy will devolve into timocracy; afterwards oligarchy; next democracy; and, finally, tyranny. Aristotle’s classification in Politics works initially in terms of two criteria: the number of members of the ruling body and whether or not the rule is “right” or “perverted” (whether it rules in the public interest, or in its own personal or class interest). Monarchy, aristocracy and polity (something like republic) can be categorized as embodying the “right” forms of government represented by, respectively, the one, the few and the many; their “perversions” are, respectively, tyranny, oligarchy and democracy. Contribution to the ends of the polis, the “good life” of the citizens, should be the basis of merit, but if one man is more able than all others at ruling, then he should be king.



For Aristotle, nevertheless, when there is a preponderance of citizens with a certain average amount of property, then a polity is both possible and desirable. The interest of those of moderate property, who are free of envy, is in conserving the polis and not in dispossessing the wealthy. Aristotle regards polity as “the practical best possible”. In fact, the basis of the classical republican conception of man is Aristotle’s: man is by nature a political animal and only where a citizen is able to take part in government and enjoy political participation can his human potential be realized (see Fink 1962).

Aristotle, though, associates democratic assembly with lawlessness or social disorder, as this was the image that democracy fifth-century Athens and first Roman Republic had. So, Aristotle’s civic humanist conception of man as a citizen allows there to be distinctions made among equals. Thus, classical republicanism is able to incorporate class division, so long as it is limited and contained by a constitution that contrives to promote the common good. It combines the optimistic aspirations of civic humanism and the classical pessimism of degeneracy in human affairs. Aristotle’s conception of the constitution (polity) was passed on to seventeenth-century Englishmen via Italian Renaissance thinkers and later to eighteenth-century Scots and Americans. The fruit of classical republicanism are found in the mixed or balanced British Constitution of 1688 (see the case of Miltonian republicanism in Armitage et al (1995)) and the American Constitution of 1789.

Machiavelli departed in the sixteenth century from the established tradition of Renaissance humanists. For him, there were no universal prescriptions for stable government but his advice to politicians was to introduce a further dynamic factor. Although princes will pay special attention to arms and to war, Machiavelli prefers

republics, with organized citizen armies defending their community and the “raison d’état”. A republic was better able to adapt itself to diverse circumstances than a prince. Republics were stronger in the defence of their freedom than were principalities, as the latter had less experience of independent institutions (see Pocock 1975).

After Machiavelli’s, two different traditions emerged: one based on the idea that the state is not an organic, natural development but the outcome of reflection and calculation, an artificial creature shaped by human minds and actions (from Hobbes to Mandeville or Bentham); and another that considered the state a natural organic institution (Hume, Burke...).

Leviathan inaugurates the modern theory of the state in the seventeenth century. For Hobbes, if the inequality of power is not resolved, it is solved by battle. An artificial man comes into existence, the body politic, with immense rights and powers. Order is established through relations of command and obedience, but political life has limited significance. Attributing limited significance to political life is also typical of Catholic Church ideology.

For Locke, the Hobbesian state of war is false. Nevertheless, without unreason and crime there would have been no inducement for mankind to move out of the early state of nature, depicted as happy. Government is also artificial. So, with regard to the constitution of the ideal commonwealth, Locke is ambiguous and, although he seems to be thinking of an unwritten constitution, he thought civil society needs a single man to give it rationality and direction.

On the contrary, Rousseau believed that the principles of political right could only be realized in small compact republics like Geneva, or in those of ancient Rome and Sparta that he so admired, as men were first of all citizens and patriots. Only in republics,

where men became the authors of their own laws, could freedom and morality be instituted. But, providing the sovereignty of the general will is not called into question, no form of government is illegitimate. As the number of supreme magistrates should be in inverse ratio to the number of citizens, in general, democratic government suits small states, aristocracy medium sized ones and monarchy large states.

Rousseau defends a conception of freedom against both Lockian individualism and arbitrary rule. Men were born free and independent individuals but obedience to a law one prescribes to oneself is freedom. He attacks Locke's modern notion of individualism as morally pernicious, and he does so in the name of the ancient liberties of classical republicanism. His Catechism of the citizen sanctifies the bonds of union and sentiments of sociability. At the heart of classical republicanism is a conception of citizenship that has expectations of political participation much beyond that of modern democratic societies (Forsyth & Keens-Soper 1988:65-6).

James Harrington indicated that monarchy became untenable in England in the seventeenth century as a consequence of the emancipation of the vassals and the rise of independent freeholders. He affirmed that the balance of power depends on that of property and that where there is equality of power there can be no monarchy. Hume criticises Harrington. In "Whether the British Government inclines more to Absolute Monarchy than to a Republic", he says that "though liberty be preferable to slavery, in almost every case; yet I should rather wish to see an absolute monarch than a republic" in Great Britain. If a single person had acquired enough power to shred Great Britain's constitution into pieces, he would really have become the absolute monarch who would not relinquish his power or establish any free

government (as the case of Oliver Cromwell had demonstrated). Therefore, Hume says, matters must be entrusted to their natural progress and operation. He recommends the sanction of antiquity. In "Idea of a Perfect Commonwealth", Hume says that a wise magistrate will never attempt experiments with forms of government merely upon the basis of supposed argument and philosophy, and he will adjust his innovations, as much as possible, to the ancient constitution.

For Hume, though it is more difficult to form a republican government in an extensive country than in a city; once it is formed, there is more chance of preserving it steady and uniform, without tumult and faction. Proximity enables citizens to mutually assist each other. Even under princes with absolute power, the local government of cities is commonly republican, while that of counties and provinces is monarchical. But these same circumstances, which facilitate the erection of commonwealths in cities, render their constitution more frail and uncertain. People living close together in a city will always make the force of popular tides very sensitive. In a large government the different parts are so distant and remote that it is very difficult to hurry them into any measures against the government.

Hayek refers to what he calls the "Mandeville — Hume — Smith — Ferguson tradition", which created an "atmosphere of evolutionary thought in the study of society". The eighteenth-century evolutionists explained how the appearance of purposefulness in the "products of civilization" could be understood as the outcome of a blind process that is not guided by foresight. This can be linked with the shaping of a new kind of republicanism, "commercial republicanism", which shifted attention to civil society as product of civilization. Commercial republicans (Ferguson, Clavière, Brissot) reconciled

morality with free market regimes based on democratic republics. Economics solidifies republics by fostering social equality, rendering all citizens fit to participate in political life. Nevertheless, commercial republicans do not give much importance to political participation. Representation is given to liberal bourgeoisie, to small, independent farmers that protect private property (see Wooton 1994 and Livesey 2001).

Actually, also monarchism can be understood from an evolutionary perspective or a conservative ideology. Edmund Burke in *Reflexions* (1790) defended the constitutional monarchy as the hereditary principle embodied in English legislation, passed on to posterity from times immemorial. For Burke, a notion of heredity gives a principle of preservation and transmission without necessarily excluding the progressive principle. Burke in *Vindication of Natural Society* (1756) presents an idealization of the state of nature where the world and all it contains were given by God to all mankind in common. But he also argues that long-lived institutions have demonstrated their utility and, moreover, the English constitution preserves unity in diversity: a hereditary crown; a hereditary nobility; a House of Commons; and people that have inherited privileges, rights to vote and liberties from a long line of ancestors. Adam Smith was very near to Burke's political ideas.

So, in Great Britain, a constitutional monarchy, linked to the preservation of liberty, is defended. John Stuart Mill in *Considerations of Representative Government* (1861) held that, although a benevolent monarchy could achieve good utilitarian results, happiness is a human conquest, consequence of the abilities of self-government and participation in public life. In a benevolent dictatorship, men's capacity to dialogue about public affairs decreases and, consequently, their moral abilities disappear.

An absolute monarchy, though, where the king claims divine rights to power, persisted in France until almost the French Revolution. Then, it alternated between monarchy and republicanism. This Revolution in France also triggered American Revolutions.

### **American Republicanism**

Conservatism is not always linked to monarchism. Note that in the USA, conservative parties are republicans, as they continue the tradition of the first 1776 revolutionaries, critical of the British monarchy (Pangle 1988, Rahe 1994). In 1776 Thomas Paine addressed his *Common Sense* to all the inhabitants of America and helped shape the US revolution against the British crown describing the hereditary monarchy as a state of oppression of kings that increased expense and unnecessary luxury. Based on this tradition, in the modern North-american constitutional theory a "republican constitutionalism" has developed (Veterli & Bryner 1996, Pope 1990). "Neo-republicanism" (Williams 1994:76) shows a communitarian and deliberative assertion that talks about a "republican freedom". Pettit (1997) says that this implies, not only non interference in accordance with the liberal paradigm, but positive freedom, as non interference would not always offer and guarantee a complete non domination.

Nevertheless, as in the USA, when independence from Spanish Crown was sought in XIXth century Hispano-American countries or in Brazil, the debate of monarchism-republicanism made nationalism and republicanism synonymous with liberalism (see Adams 1980). In Mexico, monarchism was defended by Lucas Alamán, in Chile by Benjamín Vicuña Mackena and in Argentina by Vicente Fidel López and Domingo F. Sarmiento. But the political consequences of Hispano-American independence were not just the establishment

of republican and constitutional governments in place of the Bourbon monarchy. In 1830, the continental territories that had been subject to the Spanish crown were divided into various nations. Although Spanish America had a common language and cultural heritage, it disintegrated (Rodríguez 1998). This result contrasts with the survival of the Portuguese-American colonies and with the prosperous federal union that the British colonies in America established.

In fact, after independence most of the Latin American cities or provinces preferred confederate union as a way of safeguarding their sovereign capacity. In Mexico, as Elías (1998) points out, centralists and federalists were the two wings of the republican party. The centralists criticized the federal idea for having copied the US Constitution, 1787, but federalist republicanism imposed itself in the federal Constitution, 1824 (see Archer 1994).

### **Basis for Monarchism-Republicanism Ideologies**

Some elements that constitute the basis of the defence of monarchism or republicanism can be summarized here. One, posed above, is that monarchism of a wise man is more defensible if the state is conceived of as the outcome of reflection and calculation, and not as a natural institution.

Secondly, the conception of man as a being that needs participation in the political arena to gain moral fulfilment makes it necessary to defend republicanism. Freedom, when it is not defined entirely negatively, is not the passive state of not depending on the will of another but is rather the activity of the will when not controlled. This is crucial.

Nevertheless, monarchy constitutes a federative power that gathers together different geographical regions of a nation or of various nations (as is the case with British monarch, who reigns over 16 nations, including Australia, New Zealand and

Canada). In non-monarchical countries, this power is represented by the federal or republican president. The fact that the monarch is not elected is said to dissolve independentist eagerness, since, if elected, a king would be expected to give privileges to his voters.

The Fabian Commission (2002) says that the historical firmness of the UK's hereditary monarchy has served as a powerful source of 'social glue' in a country which has always been characterised by geographic, ethnic and religious diversity and multiple identities. The monarchy provides continuity and a sense of historical stability in times of change. It is perceived to be above sectional and political interests.

Critics of republican movements also state that, as with most revolutions, republican movements lead to totalitarianism and terror, as a dramatic new creed is to be imposed. In 1789, the general populace of France wanted Liberty, Fraternity and Equality, but they got totalitarianism, as an era known as "The Terror" began, with thousands of citizens publicly beheaded. Mob rule was ended when Napoleon seized power and became the absolute ruler, not as a king but as an emperor. The Russian revolution also plunged the country into civil war, led by comrades who intended to improve the community by discarding the monarchy of the Tsars. Social chaos was ended with the appearance of an absolute monarch, Stalin. The same desire for change was the basis for the Nazi programme in the Third Reich or the killing fields in Cambodia and persuaded the Chinese Red Guard to murder authority figures in 1969.

### **Reform of the British Monarchy**

But, although it has had widespread public support, the Monarchy is actually much criticised (Freedland 1999, Picknett et al 2003, Zuckert 1994). This is especially true in the monarchies where the personal behaviour

and largely private troubles of the royal family have come to be known by all. For that reason, the Fabian Society established in 2002 an independent *Commission on the Future of the Monarchy* (cited above). The subsequent report argues that, as the existence of a hereditary unreformed apex to an otherwise democratic, pluralist state is coming to look increasingly incongruous, the monarchy needs to continue to evolve. It sets out a series of principles and recommendations for reform, although it does not discuss the merits of abolishing the monarchy or the creation of a republic. Its aim is to define the office of a head of state appropriate to modern Britain—whether a hereditary monarch or an elected president holds the office.

The report recommends clarifying constitutional role of Head of State and to ‘depoliticise’ the monarchy’s powers and duties. Also, it recommends making the monarchy more representative of a diverse Britain of many cultures and faiths, ending, for example, the historic ban on non-Anglicans, or anyone who marries a Catholic, succeeding to the throne, and the preference in the succession given to younger brothers over elder sisters; and ending the position of the head of state as Supreme Governor of the Church of England.

The Commission recommends separating the private lives of the royal family from their public duties and making the public office of head of state properly transparent, allowing, for instance, a reigning monarch to ‘retire’, rather than being required to go on till death; or requiring the monarch and royal family to pay tax on their private income and wealth. Finally, the Commission recommends professionalizing the administration of the Royal Household.

## **Monarchy in the Global Village**

In Australia, the strength of the monarchy resides in the popular belief—held since the time of Oliver Cromwell—in a “protective” institution that is above politics. However, the ties to the British Crown are decreasing, and many Australians say they are republicans. That reality led Australian politicians to hold a plebiscite in November 1999 on the possibility of establishing a Commonwealth of Australia as a republic with the Queen and Governor-General being replaced by a President appointed by a two-thirds majority of the members of the Commonwealth Parliament. The Australian Republican Movement was disappointed by the fact that the referendum on a republic was defeated with 54.87 % of the people voting against changing the Constitution. Nevertheless, this turn of event led to a World Service global debate (31st October 1999) on the future of constitutional monarchy in parliamentary democracy. On 26 June 2003 the Australian Senate requested their Legal and Constitutional References Committee to establish an ‘Inquiry into an Australian Republic’.

Republicanism in Australia is sometimes related to the rejection of traditional values and to multiculturalism, with the danger of “asianisation” (Howell 1995); or it is related to non-conservative nationalism. Australian republicans complain that British monarchy is a colonial legacy that has stunted the development of genuine Australian national culture and identity (Byrne 1995). Some critiques denounce the risk of a plunge into totalitarianism through the enactment of radical new laws, rising tensions and the polarisation of the community (Atkinson 1996). Greenwood (1999) argues the role of the Crown in the forms found in the Westminster parliamentary system better serves modern democratic government throughout the world than if it were replaced by a Presidency. A significant XXIst century

role for the Commonwealth of Nations is outlined. In New Zealand, the relevance of the monarchy has also been questioned (Miller & Cox 2001).

Apart from the countries nominally ruled by the British monarch, Belgium, Bhutan, Cambodia, Denmark, Japan, Jordan, Kuwait, Luxembourg, Monaco, Morocco, Nepal, the Netherlands, Norway, Oman, Saudi Arabia, Spain, Sweden, the United Arab Emirates, Vatican City, and other states are monarchies.

The stress of commercial republicanism is most in existence at present in Europe, the same as in the USA. The concept of "republic" and republican virtues has been revived in legal studies and political philosophy (Brugger 1999, Coats 1994, Goodwin 1995). In European states a constitutional monarchy is combined with parliaments but the monarch's duties are largely ceremonial and symbolic (Rahe 2002). In the Dutch case, some experts believe that hardcore support of the monarchy is declining (Osborn 2001). In Norway, although some polls have shown that a majority of Norwegians support holding a referendum in 2005 on monarchy versus republic, today the monarchy is in a strong position. Nevertheless, it has been subject to increasing criticism and scepticism in recent years, particularly since Crown Prince Haakon married in 2001 Mette-Marit Tjessem Høiby, an unconventional choice. In Spain after the transition to democracy, the idea of establishing a republic was rejected, not only because the previous regime had passed the baton to the monarch, who installed democracy, but also because republic was associated with instability. Two Republican periods (1873-4; and 1931-6) were aborted and, in fact, the Second Republic had a tragic end in the civil war (1936-9), which led to the Franco dictatorship (see a reevaluation by Townson 2000). Monarchy, symbol of both continuity and change, became the setting for

consensus. Republican politics has been revived by the discovery in 1997 of the diary of Manuel Azaña, President of the Second Republic.

In the Middle East, fear of the reestablishment of monarchies exists. The formation of the Islamic Republic of Iran has been accompanied by a debate with the so-called Iranian "monarchists", who are said to be a group of "technocrats" from the Shah's time, who at best tolerated the repressive political system of the Shah's monarchy, including its Savak (see Avery et al. 1993). The ongoing "war of liberation" in Iraq, waged with the intent of promulgating democracy in the Middle East, has raised serious concerns among many Arab states as to their own futures. The Saudi Arabian regime is not a constitutional but an absolute monarchy, with a hereditary leader who claims religious rights to power. Once a new regime starts to take shape in Iraq, the Saudis will be watching closely for the "domino effect" (Schwartz 2003).

Besides, in spite of being an hereditary kingdom with Islam as the only religion that may be practiced, Saudi Arabia has been America's closest ally in the Persian Gulf. The Royal Family, whose tremendous wealth depends on oil industry, has viewed America's military presence as crucial for the kingdom's security. The Saudis and the U.S. joined forces to finance Saddam Hussein's war between Iran and Iraq. Iraq's 1990 invasion of Kuwait made the Saudis invite the U.S. to move its military into their country, at first to prosecute the Gulf War, then as part of a continuing strategy to contain both Iran and Iraq (Long 1997). This decision to allow U.S. troops into the kingdom infuriated many powerful Saudis, including Osama Bin Laden, whose Al Qaeda terrorist network made a primary tenet out of the demand that the U.S. remove all forces. After the September 11 attacks, when U.S. President

decided to expand the war on terror to include Iraq in 2003, the Saudis (and most of the rest of the Middle East) refused to let the U.S. deploy troops in the kingdom for use in the conflict.

The only surviving Himalayan Buddhist kingdom, Bhutan, which had reputation of isolationism, began an opening policy after 1960's. Traditionally a decentralized theocracy and, since 1907, a monarchy, Bhutan is evolving into a constitutional monarchy with a representative government. A pro-democracy campaign emerged in 1991, which the government claimed was composed largely of Nepali immigrants. As a result, some 100,000 Nepali civil servants were encouraged to emigrate to Nepal, where they were housed in UN-administered refugee camps since 1991. A repatriation process is expected to begin in 2004. However, the Bhutanese Government finds itself facing an increased number of insurgents on the Indian side of the border. Bhutan edged closer to becoming a parliamentary democracy in 2002, when the election laws were changed so that each citizen over the age of 21 could vote by secret ballot for a representative to the National Assembly (Tshongdu) when previously, only one vote per family was allowed.

### **Some Lessons Drawn**

Subordination to historical uses is considered by the monarchists as the basis for the social order. Darwinist conservatism will defend that durable established institutions have had success, while change and transformation can be risky. European experience of constitutional monarchies shows the convenience that a political apparatus to represent the establishment or the past coexists with the one that represents the emerging progressive class.

In criticizing British Monarchy, questions of national independence and cultural identity

are drawn. If British Monarchy has served as a social glue, the case is inverse in the Middle East, where US republicanism has served as a social dissolvent and a necessary element to maintain absolute monarchy in the area.

Republicanism ideology draws the question about personal merit versus heredity class. Republicans, however, recognize differently personal merit. Firstly, classical republicanism stresses participation, secondly, liberal or commercial republicanism stress representation and the capitalistic virtues of frugality and reliability, finally, neorepublicanism stresses the dialogical virtues. Actually, the liberal republicanism has been criticized on the base of questions of personal merit by 'industrial republicans': inherited capital should not imply greater participation in management activities and corporate governance. Cooperativism defends that it is possible to create a cooperative society, as made obvious by the success of different cooperativist experiments (see the case of Spanish Mondragon experiment in Turnbull 1995). Here, the explosion of literature of the Third Way can also be recalled (Giddens 1998).

### **Internet Sites**

Monarchist. [www.monarchist.org.au/](http://www.monarchist.org.au/)  
[www.riou.org](http://www.riou.org)

Norwegian Style of Government.  
<http://odin.dep.no/odin/engelsk/norway/system/index-b-n-a.html>

Republicanism. <http://republicanism.com.au>

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## Nationalism

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### **Introduction: Nationalism in Perspective**

The idea of Nation envisages "a terminal community" to which its member owes "ultimate loyalty" and accepts its moral supremacy and authority. A member of such a nation is not only a "subject" but is under an "active obligation to the nation and its community (Young 1976:71). Nationalism then becomes an ideology of such a national community. A collective community and a social, cultural and political organization based on it and commensurate identity become the basis of nationalism. Nationalism therefore refers to identification with and "entails a submersion of one's psychological self in some greater, mass self" (Yurick 1997:205). The collective identity of nationalism may be based, in different combinations or solely on particularisms of language, common history, culture, religion, ethnicity, race, community or a political identity, for example, of a State (Jenkins & Sofos 1996:11). Thus there may be a linguistic nationalism, a cultural nationalism, an ethno-nationalism and so on. It could be based on either constitutional or ethnic patriotism.

Constitutional patriotism becomes the basis of a civic or citizenship based nationalism. Ethnic patriotism provides ideological foundations to ethno-nationalism. Whereas the former is primarily a legal-political form of nationalism, the latter is ethnicity-based and therefore cultural-political in nature. Citizenship based on law and consequent formation of a cosmopolitan "nation of citizens" evolved historically alongwith cultural and ethnicity based nationalisms in the era of modernization in Europe. (Habermas 1996:281-294) In the current epoch existence of ethnically and

culturally heterogeneous societies undermine the ethnocentric conception of nation and nationalism. Hardly any society is culturally and ethnically homogeneous. (Young 1976:184-85) Thus ethnicity-based nationalism cannot become the basis of a nation since a single uniform ethnic composition is not to be found in any given geographical-political entity. Such a nation can only be imposed either by ethnic cleansing or forcibly subsuming the minority ethnicities and cultural groups into the fold of dominant and majority ethnic and cultural group. This is well nigh difficult if not impossible in the current epoch. Multi-ethnicism or multi-culturalism are the only possibility. One of the ways this can happen is by encouraging a nationalism that is founded on cultural pluralism, co-existence and intermingling of diverse groups alongwith civic nationalism.

Multi-culturalism of culturally diverse and plural societies seeks to encourage cross-cultural dialogue to promote mutual understanding thereby negating nationalism based on mono-cultural or mono-ethnic attribute. (Gooding-Williams 2001:237) Religio-cultural diversities in plural societies have provided ideological basis for cultural nationalisms, for forging dominant culturally-oriented identities and concomitant political nationalism subjugating minority religio-cultural identities. This has created a pathological form of nationalism leading to disharmony, civil strife and disruption of democratic political processes and anomie in different societies. A new and distinct variant of nationalism and patriotism is visible in former colonies with the decline of the values of national liberation movements and anti-imperialism. It is inspired by a nationalism that verges on jingoism, quasi or soft-militarism resulting in an arms race, and emerges as a response and reaction to the real and perceived enemies across the borders.

Nation and nationalism are viewed as systems that need to be analyzed, engineered and integrated, undermining its human component. This results in authoritarian, quasi-authoritarian or totalitarian political systems in the name of nation, nation building and nationalism. Such a positivism-inspired conception undermines a democracy based on ideals of civic nationalism and individual freedom. (Srivastava 2002:71-72)

### **Classical, Moderate and Liberal Nationalisms**

Nationalism has been explained in terms of national identity, achievement and sustenance of political sovereignty. National identity is defined as rooted in "common origin, ethnicity or cultural ties". Political sovereignty is related to the formation of a nation-state. Sometimes nation as ethnic or cultural community is sought to be distinguished from State that is deemed to be a political institution. A nation in the former sense evokes intense populist sentiments. The ideological and political endeavor to claim an individual's loyalty to a nation comprising of a community of people, and often its political sovereign manifestation in form of its State, is what had been defined as nationalism.

Classical nationalism of the 19<sup>th</sup> Century comprised of a political State of a community of ethnically and culturally homogeneous people or nation defending its traditions, heritage and what were deemed to be national interests. Communities of ethnically and culturally homogeneous people to acquire a political State of their own articulated active nationalisms. However, most societies are no longer culturally and ethnically homogeneous. In fact the process of inter-mixing has been ongoing for ages only to acquire a much more rapid momentum in recent times. All such contemporary societies with nation-states formed on the basis of classical nationalism are therefore facing the

stresses and strains of such a fundamental change in their compositions. Thus the concept of classical nationalism is rather dated in the contemporary world that is becoming increasingly cosmopolitanized and globalized.

Ernest Renan, (1882) defined nation coming into existence when a group of people aligned on their own volition to form the institution of a political State. The allegiance of these people is civic and the members of this nation are citizens bound by a common political program. An ethno-nation on the other hand, is constituted by a compulsory membership based on origin, culture, language, customs and traditions. Common descent thus socializes an individual into the common culture, language, customs and traditions and thus creates ethno-cultural nation and nationalism. Former is said to have originated in Western Europe whereas latter in Germany and Central and Eastern Europe. (Kohn 1965) A nation and nationalism may have both ethno-cultural and civic attributes, yet primarily stay rooted in the former. (Seymour 2000).

Nationalism has been identified with the membership of a group of people marked by the characteristics of individuals integral to the group and not comprehensible separately. Thus the supremacy of the whole is asserted over its component parts. (Berlin 1979) The primordialist view considers ethno-cultural nations to have existed for a very long period of time in human history. Modernists, however, consider them to be of a recent origin having emerged with the rise of industrial capitalism (Gellner 1983, Hobsbawm 1990) or are just 'imagined' or constructed entities (Anderson 1965). Nationalism is also seen as a manufactured ideology associated not with the personal and automatic aspiration of individuals but with organised and structured social attributes and is thus irrational (Balibar & Wallerstein

1992). The classic or conservative form of nationalism envisages a state attached to an ethno-nation as an expression of political sovereignty (Oldenquist 1997). Such a State has to be maintained and further strengthened.

Ethno-national characters of the culture in its pure embodiment, despite the fact that they may be real or invented, constitutes the legitimization of political nationalism on ideological grounds. These cultural traits, artifacts and traditions have to be promoted by individual members as an obligation and duty towards the nation. National interests supersede all other individual interests. A moderate nationalism, on the other hand, envisages political autonomy rather than Statehood. Therefore classical nationalism is a political project in which a completely sovereign political State is controlled by ethno-cultural national group with latter under an obligation to strengthen and maintain this State. Its members are also politically obliged to adhere to, defend and strengthen the ethno-national culture.

Moderate nationalism ascribes basic political, moral and socio-cultural values to nation and nationality obliging its members to adhere to and act on them. This nationalism may be referred to as patriotism. Thus the ideology of nationalism, based on a kind of communitarianism, consider nation as a large socio-cultural group, central to political activism and of which an individual has an involuntary membership, although a voluntary acceptance of national identity by the individual is deemed preferable. In classical nationalism, in a nation-state, obligations have a legal sanction on all including individual members of the ethno-cultural entity. In moderate nationalism, it only has a moral sanction, whereas in its liberal form it is only confined to the rightful possession of a State by an ethno-cultural nation.

In varying forms nationalistic claims may supersede even human rights in its extreme variant, or in a classical form take precedence over individual interests (McIntyre 1994, A. Oldenquist 1997) or in its liberal variant provide superficial or "*prima facie* status" to the basic claims of nationalism (Tamir 1993). Universalist variant of nationalism contends that each ethno-cultural nationalism should have a State of its own whereas particularistic variant of nationalism restricts this privilege to some. Justification or acceptability of nationalism on moral grounds has always been a matter of debate. The individual's right to autonomy, for example right to privacy, and "benevolent impartiality" vis a vis ethno-cultural groups distinct from the one that constitutes the basis of existing nationalism comes in contradiction with the attributes of the classical form of nationalism. Homogeneity of a primary ethno-national culture and the nationalism associated with it undermines the diversity of a community. Creative freedom and independence of a writer, musician, literary figure or intellectual is undermined when they are enjoined, as distinct from right to "a special duty to promote national heritage".

Ethno-cultural nationalism is by definition intolerant of multiculturalism and pluralism, particularly in its classical variant. In its more extreme form particularistic nationalism in a deliberate and intentioned approach denies those very rights to others that it claims for itself. This is because of the scarcity of resources and goods as well as shortage of geographical territory in comparison to innumerable ethnic-cultural groups that exist. (Gellner 1983) Ethno-cultural nationalism is justified on the basis of communitarian premise that an individual's ethnic-cultural identity is valued, non-controversial and "good" and that a community is needed to own and strengthen it. Ethno-cultural nation is seen as the most apt form of such a

community and therefore an ethno-national political State is required to strengthen and preserve its as well as its member's ethno-cultural identity vis a vis that of others. The philosophical underpinnings of such an assertion originates from the acceptance of communitarian ethno-cultural traditions implicit in the sense of belonging and the solidarity that its members experience.

Liberal variant of nationalism may not consider these to be the core political values. It may seek an admixture of these values and those of pure individualism and cosmopolitanism, latter referring to more universalistic moral and political values irrespective of culture or geography and associated political arrangements. Liberal nationalism thus strikes a somewhat middle path. (Barber 1996). Liberal variants include contention that ethno-cultural nationalism has only superficial or notional strength; it cannot undermine individual rights; does not need a State of its own, rather a cultural autonomy instead; is subordinated to civic nationalism; its mythologies and falsehoods are allowed to be propagated only as long as they are harmless and not aggressive; and ethno-cultural nationalism's claims can only be deemed to be legitimate via free choices of concerned members of the group.

Arguments in support of ethno-cultural nationalism, in contrast to liberal variant, contend that such a community provides "natural encompassing framework" and is thus a "moral community" with shared customs and traditions, language, values, "cultural proximity" possessing an "intrinsic value" making it "valuable in and of itself". Each individual of such a community is obliged to preserve, protect, cherish and strengthen the basic features of the community, like language and customs, as distinct from those of the others. It is within the fold of such a community that an individual is thought to understand and

realize one's self-identity and values as well as those of the community. Therefore it is argued that such a community is crucial for the development of its individual component and thus such an ethno-cultural nation and nationalism is necessary. Another argument justifying such nationalism is that the particular traditions of a nation provide special moral values and thus the norms and standards of existence as distinct from general universal moral values that are rather peripheral. The identity of an individual is seen to be determined by the social and therefore communitarian environment and contexts or within the stream of national consciousness, in which he or she grows and evolves. (Nielsen 1998) An individual ought to have "a mature and stable personal identity" and commensurate morality. This could be achieved within the framework of ethno-cultural national community, that, in view of classical nationalist ought to be provided a State of their own. Liberal nationalists are, however, satisfied with some sort of political recognition and autonomy. They argue that the cultural communities be granted political protection and a "liberal political morality" be allowed to prevail.

Ethno-cultural nationalism is supported by the argument that they preserve the diversities of cultures and their uniqueness. (Berlin 1976) It has also been justified on the grounds of the popular will of the members of a community (Moore 1998); redressal of past grievances of an oppressed or victimized community, for example a minority group, or in self defense (Kukathas & Poole 2000); equality, for instance of a minority to a majority dominant community, by either granting "differential rights" (W. Kymlicka, 1995), institutional protection and minority group rights to their institutions in the spirit of multi-culturalism. (Kymlicka 2001); and the argument that the nation-states have

contributed to the growth of democracy and egalitarianism. (Miller 1995)

The meaning of classical nationalism of a nation-state based on a dominant and aggressive ethno-cultural nationalism has yielded ground to more liberal forms of nationalism reconciled to multiplicity of cultures and communities, their role in sculpting individual's social identity and creeping cosmopolitanism. It is accepting the "minimal and pluralist versions of nationalism" and a commensurate national identity. Thus the conservative classical nationalism seems to be a thing of past with the proponents of nationalism anxious to promote its more liberal versions that bears little resemblance to the former.

### ***Explaining Nationalism***

Marxist scholars consider modern nations and nationalism as a product of the epoch of capitalism resulting in the development of commerce and industry, rapidly expanding markets, greater communications, social mobility, urbanization and a common language as a basis of modern nationalism. (Jenkins & Sofos 1996:12) Other variants of nationalisms are of less concern for them. K. Marx and F. Engels were amongst the earliest scholars who linked modern nationalism to globalization and undermining of old, localistic and exclusivistic 'nationalisms':

"The need of a constantly expanding market for its products chases the bourgeoisie over the surface of the globe. It must nestle everywhere, settle everywhere, establish connections everywhere. The bourgeoisie has through its exploitation of the world market given a cosmopolitan character to production and consumption in every country .... In place of the old local and national seclusion and self-sufficiency, we have intercourse in every direction,

universal interdependence of nations. And as in material, so also in intellectual production .... National one-sidedness and narrowmindedness become more and more impossible" (Marx & Engels 1962:37-38)

Hegel characterized nationalism as "popular spirit". This was associated to his idea of "world spirit" or Geist. Former represented the national identity consistent with the emerging capitalism and bourgeoisie or the idea of modern nation, whereas the latter referred to cosmopolitanism or globalism. Adorno, Horkheimer and Marcuse argued that collective identity based nationalism of extreme variant like Nazism and Fascism undermined individuality. Individual rights and interests were subordinated to national interests and such nationalisms "facilitated the manipulation of men in the interests of collective". (Stirk 2000:176-181) Taken to the extreme, individuality was subsumed under the overarching, all-encompassing and pervasive ideology of a particular variety of perverse and totalistic nationalism.

Three types of political nationalisms have been identified: one, as exemplified and inspired by American and French revolutions that signified victory of democracy over autocracy and monarchical rule; two, post-colonial nationalisms in Asia and Africa that were the products of protracted national-liberation or anti-imperialistic struggles against European colonizers; and thirdly, chauvinistic nationalisms based on racial supremacy or ethnic exclusivity like in Nazi Germany or Balkan or Balkan conflicts. (Holton 1998:136) First one is associated with the emancipatory variant of civic nationalism that sought to anchor itself in liberty, equality and freedom based on the premises of liberal democracy and rise of capitalism. Second type rooted itself in a

variant of civic nationalism that is greatly inspired and influenced by the ideas of socialism and a desire for equality, freedom, emancipation of subjugated people and economic progress. Third variant is totalitarian, illiberal and against individuality and individual freedom.

Ernest Gellner (1994) characterized ethnographic nationalisms as "the study, codification and idealization of peasant cultures in the interest of forging a new national culture", (Gellner 1994:29) whereby a self-conscious ethnic group defines its ethnic boundary as a political one. Thus the modern or civic nationalism was consistent with an industrial society unlike other nationalisms that were the ideological spillovers of the ethno-cultural and political formations of a pre-modern agrarian society. (pp. 33-35) An ethnically constituting the basis of ethno-cultural nationalisms is said to possess

"a collective name, a common myth of descent, a shared history, a distinctive shared culture, an association with a specific territory and a sense of solidarity." (Smith 1986:19)

Ethno-cultural nationalism of a classical and conservative kind has often provided a readymade ideological basis for political mobilization against the civic form of nationalism.

Civic or citizen-oriented nationalism that coincided with a democratic political system with emancipatory content has, however, over a period of time, transformed itself into conservative model of citizenship seeking unquestioning allegiance to the nation-state. Such a model of nationalism homogenizes the concept of citizenship as if it is composed of "a socially undifferentiated citizenry defined first and foremost by their membership of a 'nation'". Political and legal identification, homogenization as citizens of a nation and as compulsory members of a nation-state that is deemed to be an eternal community and

politico-legal arrangements ignores social, economic and cultural distinctions within a given society. This restricts the scope of free expression of dissent as well as differences and acceptance of a variegated differentiation of diversities—political, social, cultural and economic in a given society.

A populist variant of "proto-fascist" nationalism based on "ethnic and cultural determinism" instead of "open citizenship" considers as "aliens" certain other religious, social or political groups, like minority communities, liberals, parliamentarians, communists, socialists, trade unionists, feminists as "unpatriotic". This underscores the contradiction between civic nationalism of a democratic variant and 'ethnic and cultural particularisms' based nationalisms. Conservative variant of nationalism is close to the political manifestation of such nationalism. It seeks to deny the given diversity of a society and resists the democratic evolution of the concept of citizenship by insisting that an uncritical loyalty to the nation and its State is synonymous to the civic form of nationalism based on "open citizenship". Nation is thus identified as terminal community and nationalism as terminal ideology for all times to come. Civic nationalism of an evolutionary variant led to democratic reforms and acceptance of multi-culturalism. The cultural/ethnic/ideological nationalism provided a basis for fascism, chauvinism, ethnic cleansing, militarism, conservatism and cultural fundamentalism (Jenkins et al 1996:20-21).

Religious ideologies and leaderships create community identities (Hasan 1994:59) and can provide an ideological grounding for a religion based cultural nationalism. A religio-cultural nationalism is primarily anti-minority, particularly against minority religions and the cultures associated with them. The ideology and politics of cultural

nationalism based on religious distinctions too has a propensity of being proto-fascist and anti-democratic.

Nationalisms and national identity are sculpted on a selective version of history, a particular historic imagery and invented traditions (Lunn in Jenkins et al 1996:86). Such a selectivity is practiced in case of all types of nationalisms. Even the political nationalism of a modern nation-state carefully chooses its heroes, selections from its history, cultural and patriotic symbols, and designs and customizes its traditions to define its nationalism and nationhood. The western concept of a nation-state had sought an overlap between language, religion and political sovereignty resulting in suppressing of certain nationalities, their languages and cultures, when the modern nation-state took shape. (Gupta 1997:228) This provided space and possibility for nationalisms based on "ethnic and cultural particularisms" to assert themselves. A civic or citizen-oriented democratic nationalism does coexist and combines with specific socio-cultural features of a given society and nation. However, attempts to impose and assert nationalisms based on "ethnic and cultural particularisms" have an anti-democratic content inherent unto them.

In some countries that adhere to ethnicity-driven nationalism, citizenship can be acquired by virtue of common descent or stock. This can be referred to as "nationalist conception of citizenship" whereby not only cultural but 'blood' or genetic ties constitute the basis of an ethnically defined membership. (Hampton 1998:221-224) Nationalist citizenship based on genetic ties may not be anti-democratic per se, but it has a propensity to develop into more chauvinistic form of nationalism and even fascism. This variant of nationalism only grants membership of a nation on the basis of genetic commonality as distinct from "open

citizenship". According to Eric Hobsbawm, there is an "attempt to structure atleast some parts of social life within .. ( 'the constant change and innovation of the modern world') .. as unchanging and invariant". This provides the cultural basis of nationalism, like for example, English nationalism and the English pride and identity. Such an assertion could have racial underpinnings (Jenkins & Sofos 1996:83-88).

Race or 'new racism' has been the basis of crudely chauvinistic nationalism informing the ideology of ultra-nationalist right-wing organizations based on the distinction of the color of the skin. It has a cultural as well as a biological dimension. The biological distinction based on the perceived superiority and inferiority of the color of the skin is sought to be associated with superior and inferior types of cultures. Thus the notional superiority of the color color of the and associated culture becomes the basis of defining nationalism. There is a tendency "to create a congruence between membership of the political nation-state and identification with a national culture, a way of life" (Evans 1999:1) Individuals not socialized in such a "national culture" and "way of life" remained outside the ideological boundaries of nationalism defined on such precepts. This may result in chauvinistic variants of nationalism if a 'national culture' bases itself on an exclusive and narrow interpretation of "national culture".

Nations have been seen as 'imagined communities' or 'imagined' bonds of human association and nationalism as its ideology. Even the limitations of political nationalism have been pointed out by highlighting that nations and nationalisms are 'imagined' political entities. They exist, first and foremost, in the minds of the people who adhere to the ideology of nationalism. These are therefore, even in their democratic and civic form, rather narrow concepts limiting



people and their 'imaginings' to politico-geographical territories that confine and bound them. A history, a territory, a set of traditions and symbols are produced to construct and imagine a nation and its nationalism. These bonds are formed on a territorial basis to constitute the modern nation-state. A territory is historicized and its inhabitants are territorialized to form a nation. Each nation has its own distinct and selective identification in terms of "traditions, museums, monuments and ceremonies" to give it a unique character of its own. Cultural characteristics, images and narratives give a nation and its nationalism its distinctive feature. Modern nation and nationalism is a recent phenomenon. The paradox of the modern nation remains that it makes a selective use of the traditions and the past to justify the contemporary social arrangements of a nation. Traditions are often used to mobilise 'modern' nation and nationalism (Evans 1999:1-2). Nationalism therefore has a socio-cultural component. Cultural symbolism may be however used to invoke attachment to a chauvinistic form of undesirable nationalism.

It has been a matter of debate in recent times as to whether the modern nation-state and the ideology of nationalism associated with it has lost its relevance. It certainly seems to have lost its revolutionary and progressive content it was imbued with at the turn of last century and when colonies threw off their yoke, one after the other. In recent times the concept of civic nationalism associated modern nation-state has been challenged by an ethnicity-based regional and localized nationalism. Modernization is viewed as being synonymous to westernism. Citizen-based civic nationalism has been often identified with westernism and a political system associated with it. Even religion is being used to challenge civic nationalism and bring about a revival of

localism of a narrow variant. Localisms based on ethnicity of national, regional and sub-regional types have been on the rise in recent decades. Concept of citizen-based civic nationalism and political system has been challenged by localized nationalisms rooted in religion, ethnicity, regionalisms, race and other socio-cultural attributes.

Nationalism is "a manipulated false consciousness" for Marxist scholars. Nationalism therefore for them is only a partial representation of one's existence. It prevents members of a nation or citizens from a complete and total understanding of their own selves and true socio-economic conditions. Therefore for Marxists, the idea of nationalism has only partial value and is certainly not a terminal concept of political organization and existence. Civic or citizen-oriented nationalism gave its members political rights, but not complete socio-economic rights that are hemmed in or restricted because of the class divisions in any given society and nation. Nationalism of newly independent colonies was like the European nationalism of initial phase and was progressive in nature. This was in contrast to the 'reactionary' nationalism of dominant nations (Evans 1999:11-12). However, this form of nationalism too has become ossified and static in form as well as content. The distinctiveness of cultural plurality constituting different nations and nationalism became a key feature informing the nature of contemporary relationships between nations. (Said 1989) Such a nationalism alongwith social distinctiveness not only provided a sort of distinctive national identification, but also became a source of comfortable community identity in its moderate form. Thus, by and large civic nationalism coexisted in practice with distinct socio-economic flavor in its moderate and non-chauvinistic form.

The process of economic and cultural globalization however, is gradually producing

a form of "world cultural convergence" with a "shared culture" and a common "world awareness" (Said 1989:21). Local and national is tending to become global and cosmopolitan. All this is certainly impacting the understanding of nation and nationalism as we have understood for long. Religion too had been associated to the processes and dynamics of nation-formation and the concept of nationalism with the belief that the modern nations emerged on the ruins of mediaeval Christendom (Gellner 1994:18). It has been, however, contended that modern nation and nationalism is a political phenomenon of much later day and age (p.22). It seems to be encountering the prospect of being overtaken by an ever-increasing process of globalism and globalization whereby the time and space are getting increasingly compressed as the World comes infinitely closer.

## **Conclusion**

Nationalism is the ideology of a nation-state justifying the collective group identity of a nation and its ethical-juridical supremacy over its constituent members. Individual identity is subordinated in varying degrees to this greater mass identity. The basis of this collective identity are either particularisms of language, culture, ethnicity, race, religion and so on, together in varying combinations or separately, or the constitutional patriotism or legal or civic or citizen-based nationalism of a modern nation-state.

Ethno-cultural nationalism and a cosmopolitan "nation of citizens" evolved historically almost simultaneously with the emergence and growth of modernization in Europe of industrial era. Contemporary societies are more heterogeneous ethnically and culturally, therefore undermining the prospects of nationalism of the former kind. A secular form of civic nationalism is a more feasible proposition incorporating multi-ethnicism and multi-culturalism in most

present day societies. Attempts to foster religio-cultural or ethno-cultural nationalisms of dominant ethnicities, cultures and religions have resulted in civil strifes, disharmony and anomie.

Primordialists contend that the ethno-cultural nation existed for times immemorial, whereas modernists argue that they emerged with the rise of industrial capitalism. Classical nationalism in its conservative sense incorporates the idea of formation of a national identity alongwith political sovereignty based on a State. It is a combination of ethno-cultural nationalism and a political sovereign State. It often tended to mean an individual's loyalty to the State representing the political sovereignty of its nation. Individual's allegiance to its ethno-cultural nation and nationalism degenerated into obedience to its state that had to be not only preserved, continually strengthened and perfected. Such a State demands its citizen's unflinching devotion to itself resulting in authoritarianism and totalitarianism. Classical nationalism, over a period of time, developed a strongly conservative content. It often rationalized and justified explicitly authoritarian and totalitarian political systems.

The basis of ethno-cultural nation and nationalism is compulsory and not voluntary membership of an individual to the collectivity. This in itself provides a rather illiberal and authoritarian basis to such nationalism. A moderate variant of nationalism is satisfied with political autonomy instead of its own State for an ethno-cultural nation. It seeks moral sanction as far as the obligations of its members are concerned rather than the legal sanction sought by classical form of nationalism. Liberal form of nationalism seeks to combine the values of ethno-cultural nationalism with individualism and universal moral and political values of cosmopolitanism. Classical

nationalism of a conservative variant is an anachronism to the modern day multi-ethnic, multi-cultural and pluralist societies. Liberal nationalism is an ideological response to the outdated and obsolete conservative classical nationalism and is more in tune with modern-day capitalism, rapidly globalizing and cosmopolitan world and its component multi-ethnic, multi-cultural societies.

A nationalism that is emancipatory, cosmopolitan, egalitarian and of democratic persuasion, guaranteeing individual and human rights and freedom and takes into consideration the existing socio-economic and cultural differentiation in a society can only provide the most suitable form of nationalism in the era of globalization. Nationalism is not a terminal form of political concept in long-term historical span. With political evolution, it is likely to give way to more cosmopolitanized forms of political concepts and organizations in future. However, for the foreseeable future, nations and nationalisms are there to stay. Nationalism, and what form it should take, will continue to be debated.

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## Neoliberalism and Washington Consensus

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### Introduction

The debate about the term ‘Washington Consensus’ was coined in 1989 by John Williamson (Williamson (2004a). It was introduced in a period when the Keynesian dominance in economic theory and policy had collapsed—after the mid-1970s crisis and Keynesianism’s apparent inability to solve it—and neo-liberalism (promoted by the Reagan and Thatcher administrations in the US and the UK respectively) had become the new orthodoxy.

Williamson’s aim was to codify that part of the neo-liberal analysis and policy proposals which have become commonly accepted within Development Theory and particularly in the circles of the big developmental institutions (primarily the IMF and the World Bank) seated in Washington. In Williamson’s (2000:254) own words his effort ‘was an attempt to distil which of the policy initiatives that have emanated from Washington during the years of conservative ideology had won inclusion in the intellectual mainstream rather than being cast aside once Ronald Reagan was no longer on the political scene’. Thus, ‘Washington’ refers to the influential circles and institutions based in Washington. And ‘Consensus’ refers to the part of neo-liberal policy prescriptions that had been widely accepted.

There is another geographical dimension in the term ‘Washington Consensus’. Its policy prescriptions were primarily issued for the Latin American economies in the 1990s, although they subsequently spread to the rest of the developing and less developed countries. Again in Williamson’s (2000:251) own words, the term refers ‘to the lowest common denominator of policy advice being

addressed by the Washington-based institutions to Latin American countries as of 1989’. Williamson (1990, 2000, p.252-3) summarizes these policy prescriptions in ten propositions:

- 1) The imposition of *fiscal discipline*.
- 2) The *redirection of public expenditure priorities* towards other fields.
- 3) The introduction of *tax reforms* that would lower marginal rates and broaden the tax base.
- 4) The *liberalization of the interest rate*.
- 5) A *competitive exchange rate*.
- 6) The *liberalization of trade*
- 7) The *liberalization of foreign direct investment inflows*.
- 8) The *privatization* of state-owned economic enterprises.
- 9) The *deregulation* of economic activities.
- 10) The creation of a *secure environment for property rights*.

The theoretical foundations of these proposals can be easily discerned. They are the usual analyses advanced by neo-liberal economic theory. Economies are in crisis because of impediments to the free operation of the market. The impediments came from the overinflated interventionist Keynesian state and its expansionary and redistributive policies that deform market data and signals. The solution, according to the neo-liberal mantra, would be the withdrawal of the state from the economy and the reinstatement of the unhindered operation of the market. Therefore, fiscal discipline should be imposed on public activities and a return to the balanced budgets (as opposed to the Keynesian deficit and expansionary budgets). The now limited public expenditure should be directed towards fields that cover its cost (possibly through the imposition of compensative payments) and would support private entrepreneurship instead of paying for public works and redistributive policies. Subsequently, the tax system should be

reformed so as not to hit hard business profits and the incomes of the upper strata, which were conceived as the locomotive of the economy. After all, the limited public expenditure can do with less taxes. Additionally, the operation of the financial system should be liberated from the state grip and prerogatives and be left to the free operation of the market forces. Thus, the interest rate should be determined more or less competitively. The withdrawal of the state from the economy required, also, the privatization of all the activities and enterprises that were state-owned and directed, the limitation to a minimum of all state regulations and adequate guarantees that there won't be any violations of property rights (as it had happened previously with nationalisations etc.). With the advent of the second generation of neo-liberal theories, which emphasised the opening of the economies, the previous set of policy proposals was supplemented with three others that aimed to the liberalisation of international trade, capital movements and financial activities. Thus, protectionist measures had to be abolished and free trade movements established. Also, the free international movement of capital investments had to be secured. And, last but not least, international financial transactions and, primarily, the exchange rate of the currency had to be set according to market prerogatives and not by state policies.

### **Consequences of Washington Consensus**

There is a heated debate on whether the Washington Consensus promoted the development of developing and less developed economies or not. Today there is a widespread perception that it failed and that it led to crises and impoverishment. It would not be unfair to state that the term truly carries a bad reputation. This is accepted even by its defenders as, for example, by Naim

(2002) who acknowledged that the Washington Consensus is a 'damaged brand name'. Criticisms and the concomitant bad reputation do not stem only from theoretical and ideological opposition to the Washington Consensus but, most of all, from a series of persisting problems and crises that are, rightly or wrongly, associated with it.

### **Imposition of Neoliberalism in Developing Countries**

All these ideas, associated to the 'Washington Consensus' had already been established as the orthodoxy in the developed countries in the 1980s. What the Washington Consensus aimed to do was to introduce them in the developing and less developed countries. As Williamson explicitly stated, there appeared to be a sort of global apartheid, which claimed that developing countries came from a different universe which enabled them to benefit from (a) inflation (so as to reap the inflation tax and boost investment); (b) a leading role for the state in initiating industrialization; and (c) import substitution. The Washington Consensus aimed to break this differentiation.

Quite soon, after its formal declaration, the Washington Consensus came under criticism from many quarters. These criticisms emanated from mainstream economics (Atkinson 1999b, Rodrik 1992,2002,2003) and particularly a current associated with the work of J.Stiglitz (1998a,1998b) as well as from Marxist Political Economy (Fine 2001a,b,2002, & Shaikh 2003,2004). An important point in this controversy was the very definition of the term 'Washington Consensus'. For nearly all its critics the term was synonymous with neo-liberalism and a blind fundamentalism of the market.

Williamson (1997,2000,2004a,b) made a feeble defence of his term arguing rather unconvincingly that it was not in his intentions a so close identification of the term

with neo-liberalism. He maintained that he simply codified the consensus view within the big Washington institutions and his concept was a mere technocratic formulation devoid of ideological and political motivation. He also argued that his 'Washington Consensus' was not even a policy prescription but simply a list of policy reforms; although he is sympathetic to the former view and he accepts that at the time of the introduction of the term these two coincided (Williamson 2004b). However, he added that his definition might be problematic in some aspects and that he himself had reservations on some of these. For example, in retrospect, he doubts whether Washington institutions unanimously favoured the competitively determined exchange rate and the rapid abolition of capital controls. His reservations with the Washington Consensus' policies were that their poverty reduction policies had to be more emphasized and sophisticated and that a greater emphasis should be put upon institutions and their role.

Despite Williamson's arguments it cannot be denied—and even he cannot reject altogether—that the Washington Consensus has a definite ideological and political background: that of the neo-conservative policies of the last quarter of the 20<sup>th</sup> century. Furthermore, the Washington Consensus cannot be delegated to a simple sum of policy proposals. It has definitely a spinal column on the basis of which the whole edifice has been constructed. This is implicitly accepted even by Williamson who, in many papers, argues that there are three big ideas behind the Washington Consensus: macroeconomic discipline, market economy and opening of the economy (at least in respect of trade and foreign direct investment). Washington Consensus' macroeconomic discipline is of a particular type and has specific priorities that differentiate it from other types of macroeconomic orderly state of affairs. It has

certainly nothing to do either with Keynesian macroeconomic prerogatives or with those of other more radical perspectives. In almost all cases it led to austerity budgets and policies that favoured the wealthier and worsen the position of the lower strata. The same holds for the push towards a market economy and the opening of the economy. The first stems from a neoconservative conception of the economic role of the state and of its alleged inability to manage properly the economy. The second has the same origins complemented with the simplistic belief that it will lead to increased competition and thus consumers will in the end be better off. As it will be shown in the following sections of this chapter, these had the same negative effects as the first big idea. In this sense, the Washington Consensus is a perspective that dictated a policy prescription. Indeed, under its auspices, numerous reform programs were imposed—willingly or unwillingly—on less developed or developing countries.

The controversy about the definition established rightfully a meaning for the term. The actual content of a term is not given by the intentions of its founders but by the broader socio-political environment and the practical outcomes of the policies dictated by the term. On these grounds, it is overwhelmingly clear that in the 1980s and 1990s (there predominated in official circles a current), that considered as its main task the abolition of the state-run development policies and the restoration of the free operation of the market regardless of costs and special features of the developing economies. This line of thought was clearly associated with neo-liberal theory and the Washington Consensus was its arm in the field of Development theory and policy. Consequently, the discussion of the concept cannot be constrained to the limited agenda of issues that its creator proposed but must encompass the whole spectrum of the relevant

theory and applications. Williamson (2002) himself soon conceded the argument accepting that, since that the term became public property, its meaning is being set by the wider perception about it. Therefore, he declared that there is no meaning in struggling for the content of the term and called for an issue-by-issue discussion of the proposed policies.

### *Poverty, Catch-Up and Social Upheaval*

After the first years of implementation of Washington Consensus policies and reforms there was a growing sense, among friends and foes, that it failed its promises. More specifically, from the late 1990s and onwards, the Washington Consensus was facing major difficulties regarding a number of issues, which were not included in its declared objectives but are crucial for the development process. It was criticized for failing to organize a 'human face' adjustment process and, thus, for causing social upheavals. Additionally, it was criticized for failing to deliver significant advances in performance, let alone development. Several studies argued that its policies led to an increase in poverty and inequality both between developed and developing and less developed economies and within themselves. Additionally, the apparent inability of developing and less developed economies to catch-up the level of growth of the developed ones and, in many cases, the increase of the gap between them were attributed also to the policies instigated by the Washington Consensus.

The first criticism, 'adjustment with a human face', touched upon the many cases where reforms dictated by the Washington Consensus had led to abrupt changes and a disruption of social cohesion. The imperatives of the Washington Consensus' policies were usually implemented in a technocratic manner, disregarding social and political complexities. This, in return, created major

problems and led to social and political upheaval. This was particularly true in cases of 'shock treatment' reforms.

The aforementioned criticism was also closely linked to the second one, i.e. the inability to exhibit an unambiguously better economic performance and to promote development. Issues of poverty, the environment, and of women's position, had been overlooked drawing criticism over both the desirability and the efficacy of adjustment policies.

Moreover, for almost all critics, Washington Consensus' inability to address issues of poverty and inequality lays in its analytical perspective and are considered as its most important deficiency (see Atkinson 1999a). The Washington Consensus held the view that poverty and inequality problems were of a secondary order, which more or less would have been alleviated once the market was free to operate undisturbed by the impediments of ineffective state intervention. In particular, it was thought that if the domestic markets were liberated from any impediments, then the free operation of capital, domestically, but mainly internationally will provide all the stimulation and the efficiency necessary for feasible development (see Kozul-Wright & Rayment (2004)).

Against this market-fundamentalist presumption, most of the critics point out that, (during the last twenty years of the 20<sup>th</sup> century after the implementation of Washington Consensus' policies and structural changes), there was a marked increase of poverty and inequality (see Chossudovsky 1997). Critics coming from the Marxist Political Economy stream attribute this upsurge to the class nature of the Washington Consensus, i.e. that it is a set of policies that promotes capitalist interests and especially the interests of big imperialist powers. Some mainstream critics argue that



advocates of the Washington Consensus confront only the so-called 'traditional causes' of inequality (such as land concentration, dominance of natural resources, unequal access to education, and urban bias (in pricing policies, allocation of public expenditure and investment and so on)). For them, while such traditional factors were clearly responsible for the high-income concentration observed in the 1950s through 1970s and their persistence at a high level in the subsequent two decades, they cannot (with the possible exception, in some regions, of educational inequality) explain the widespread surge in inequality observed over the past twenty years of the Washington Consensus. Instead, several 'new' factors – such as technological changes with 'new technologies' generating a demand for skills and an earnings distribution more skewed than the emanating 'old technologies' - have had more relevance to the recent rise in inequality. This critique might be pertinent but it is beyond doubt that the Washington Consensus cannot address even the 'traditional causes' of inequality.

### *Crises of the 1990s*

The problems mentioned above were brought forward and emphasized in the mid-1990s after a series of crises in the developing world: the 1994-5 Mexican 'Tequila' crisis, the 1997 Asian crisis, the 1997-9 Russian 'Vodka' crisis, the 1998 Brazilian crisis and finally the 2000 Argentinean crisis. In all these cases, the Washington Consensus policy prescriptions were blamed since these crises happened while these countries were implementing its policies and structural reforms. A common feature of all these cases is that they ended up as exchange rate crises. However, it is also true that each case had its own specific characteristics.

In the first case, Mexico, the problems were caused by the attempt to open the

economy and introduce financial liberalisation. This led to the collapse of the peso and the default of the Mexican debt. In the Asian case the crisis was caused by the attempts to conform to an international environment a-la Washington Consensus and at the same time to reform their internal structure away from the Asian developmental model and towards the Washington Consensus prescriptions. The crisis took again the form of an exchange rate crisis and led to abrupt abandonment of these reforms. The Russian case is different since it stems from the transition process towards a market economy. Shock adjustment policies, the opening of the economy and its increased financialization made it vulnerable to contagion effects of the Asian crisis. This caused the collapse of the stock market, subsequent devaluations of the rouble and finally the suspension of its convertibility. In the Brazilian case the attempt to introduce financial liberalisation backfired. The imposition of fiscal discipline by redirecting public expenditure towards other fields and the reform of the tax system towards Washington Consensus standards demolished the Brazilian fiscal and tax system. This led to an exchange rate crisis again. Finally, the Argentinean case encompasses all the features of the Washington Consensus prescription. It began with an ambitious plan of Budget, trade and monetary reform and quite proceeded to a currency board, i.e. the pegging of the peso to the US dollar on an one-to-one basis. These reforms created serious problems in the economy and led to the biggest sovereign default in modern history.

### **Washington Consensus Friends and Foes**

Three broad streams can be discerned regarding the evaluation of the Washington Consensus. The first stream encompasses its defenders and supports, critically or

uncritically, its legacy. The second one stems also from neoclassical economic theory but assesses negatively the impact of the Washington Consensus and also disputes part of its analytical framework. This second stream is associated with the post-Washington Consensus argument. Finally, there is a third stream coming from Marxist and Radical Political Economy that not only assesses negatively the impact of the Washington Consensus but also adheres to a completely opposite analytical and ideological perspective.

### **Reformists and Fundamentalists**

Supporters of the Washington Consensus are divided in two camps. The first one comprises of the fundamentalists which argue that the failures of the Washington Consensus were the result of faulty implementation and reluctant reformers (e.g. Krueger (2000), Franco (1999)). The second camp argues that there should be 'a reform of the reforms', i.e. that despite Washington Consensus merits it is necessary a reappraisal of its agenda (e.g. Kuczynski & Williamson 2003, ECLAC 1995, French-Davis 2000).

For the fundamentalists both the neo-liberal character and the policy prescriptions are correct. What went wrong is the way they were applied. Thus, in pushing through the reforms careful consideration has to be given to state capacity, bureaucratic constraints and agency problems. Issues of effective governance and even 'second-best options' have to be taken into account. There is, however, a new element that creeps in their defence of the Washington Consensus. By focusing on these issues, they have to pay attention to the role of the institutions; an element rather alien to the pure versions of the neo-liberal approach.

However, a growing majority of the adherents to the Washington Consensus recognizes that its problems are much more

serious than simply implementation errors. This approach has been enforced by internal disagreements within mainstream economics. The poor record of the Washington Consensus has caused significant uneasiness within the mainstream, which culminated, from the mid-1990s and onwards, to a series of critiques (e.g. Fisher (2003), Krugman (1990), Rodrik (1992), Sachs (1987)). For these critics the original version is too rigid (by disregarding intermediate positions between the extremes of indiscriminate liberalization and arbitrary interventionism) and jumps to policy recommendations based simply on the maximization of liberalization. Thus, a search for a reformist version began. Several versions of this have been proposed ('reform of the reforms', 'augmented Washington Consensus' etc.). Williamson (2003:237) himself led this process by acknowledging that the results of even his definition of the Washington Consensus have been disappointing for three main reasons:

1) As proved by the series of crises, the Washington Consensus did not emphasize crisis avoidance. Additionally, it is guilty for reckless enthusiasm for capital account liberalization.

2) The reforms were incomplete, particularly regarding the labour market where dualism persisted. Also fiscal reform did eliminate budget deficits but did not manage to create in good times surpluses as a buffer for bad times when deficit spending is required. Additionally, there was a disregard for reform of institutions and good governance.

3) The objectives of the reforms were narrow (simply to restore growth) without concern for employment, income distribution, poverty and other social issues.

However, he argues that these failures do not necessitate the abandonment of the Washington Consensus, nor giving socialism another chance or introducing industrial

policy or closing the economy. For Williamson (2003:330), the way forward is to liberalise the labour market but in a civilized way, to improve income distribution and to recognize the role of institutions. He even plays down the differences with the post-Washington Consensus critics by arguing that their sole difference is that the latter presents its agenda as a repudiation of the WC whereas he argues for its continuation and reform. Similarly, Williamson (2004b, p.1) applauds – with minor corrections – Rodrik’s (2002) Augmented Washington Consensus, despite the latter’s explicit rejection of its feasibility (see Rodrik (2002, p.1). Rodrik has argued that in the end of the 1990s a revised version of the Washington Consensus emerged, which augmented the initial agenda with the following items:

- 1) Corporate governance
- 2) Anti-corruption
- 3) Flexible labor markets
- 4) WTO agreements
- 5) Financial codes and standards
- 6) ‘Prudent’ capital-account opening
- 7) Non-intermediate exchange rate regimes
- 8) Independent central banks/inflation targeting
- 9) Social safety nets
- 10) Targeted poverty reduction

In a similar vein, Ffrench-Davis (2000) and ECLAC (1995) offer a mixed account of the impact of Washington Consensus reforms on Latin American economies and argue for the need of a ‘reform of the reforms’. For them, the initial reforms imposed macroeconomic discipline on local authorities, defeated hyperinflation, improved budget balances and fiscal savings and promoted exports. On the other hand, new imbalances were caused (particularly regarding the external sector), policies were too rigid and could not adapt to changes in the macroeconomy and social dimensions were neglected, thus causing social clashes.

To a large extent the reformists attempt to drop the overtly neo-liberal character of the Washington Consensus by attacking neo-liberal fundamentalism and arguing for a practical policy-oriented debate rather than ideological and general-theoretical controversies. They also emphasize the role of institutions – which is a shy alias to the state – and the importance of social issues (such as poverty and equity). They, therefore, concur – setting aside individual grievances – with aspects of the post-Washington Consensus thesis although they, usually, reject the label.

### **Post-Washington Consensus: Critique from Within**

The post-Washington Consensus thesis, launched in 1998 by Joseph Stiglitz, is the most ambitious attempt to resolve the Washington Consensus problems, from within mainstream economics. What distinguishes it from other mainstream critiques of the Washington Consensus is that it is sharply critical of the latter and that it is based on a differentiated analytical approach, the ‘economics of information’. According to Stiglitz (1989), there is no perfect information, as the neoclassical mainstream stresses. Instead, informational asymmetries exist which allow for transaction costs and market imperfections. Thus, the definition of market imperfection is broadened and the argument for state intervention to mitigate them is reinforced. This contrasts directly with the Washington Consensus, where the state is not seen as a corrective power. It contrasts also with the old Keynesian big government policies. The early Keynesian opposition to the Washington Consensus has often accepted the latter’s terms of debate, i.e. to counterpose the state and the market and to favour state intervention whether in getting prices wrong, picking winners, or guiding the private sector through public expenditure. On

the contrary, for Stiglitz (1998a, p.25) there cannot be a return to old Keynesian policies but the state must focus exclusively on what he calls fundamentals, i.e. economic policies, appropriate regulation, industrial policy, social protection, basic education, health, infrastructure, law and order, environmental protection. For him the question is not whether the state should or should not be involved, but rather the question of how it should be involved. His main argument is that the state is not anti-market force but a complementary one.

On this alternative analytical approach are based the 'New Development Economics' (Nobel 2001) and the post-Washington Consensus, which emphasise history and institutions. Through the emphasis on institutions it attempts to bring the social dimension back into the analysis as the means of addressing, and potentially correcting, market imperfections. It also aims to differentiate itself from old Keynesian statism.

For Stiglitz (1994,1998a,1998b) the Washington Consensus fails because the simple liberalization of markets does not suffice for their normal operation, particularly in the developing countries. The existence of information asymmetries, that prevent markets from allocating resources efficiently, and the lack of complete and efficient institutional systems to mitigate these asymmetries are the causes of this failure. Thus, development policy should not aim only to the markets but also to the institutions. In a sense, the post-Washington Consensus shares the same agenda with its predecessor but with some crucial modifications. The removal of the constraints and controls on the markets and the international capital mobility and privatizations should be done through a smooth and gradual process and by taking into account the specific historical and social

situations. Essential part of this process is the creation of new institutional regulatory frameworks that can guide, correct and control the market. Moreover, more room is allowed for discretionary and active policies. On top of all these, Stiglitz rejects the Washington Consensus monistic focus on fighting inflation and puts priority on the stabilization of output and the promotion of long-run growth (through education, transfer of technology and several other channels that are being neglected by the Washington Consensus). Finally, he emphasizes the role of the financial system (the 'brain' of the economy) and argues that the aim should not be a liberalized financial system but a properly regulated and efficient one.

### ***Radical Critique***

There is also a more radical critique of both the Washington and the post-Washington Consensuses coming from the Marxist Political Economy. This approach follows a different analytical course by focusing on social classes and the struggle between them rather than on maximising individuals (as both Consensuses do). In this context the Washington Consensus is a vehicle for the exertion of imperialist dominance by the developed capitalist economies (and primarily the US) over the developing and less developed countries. Its set of policies advances the specific interests of these economies, which are similarly advanced with the so-called globalisation.

Thus, Shaikh (2003, 2004) disputes that trade and financial liberalisation promotes development, as both the Washington and the post-Washington Consensus (more qualified) believe. Empirically, today developed economies have, in the past, systematically used activist and protectionist trade and financial policies in order to attain their present status and, in many cases, they continue to follow them. Also, as even

mainstreamers accept (e.g. Rodrik (2001), p.7), it has been proven that liberalisation policies do not lead to higher growth rates. Thus, the pressure to liberalise favours the developed countries over the developing ones by preventing the latter from following the path of the former. Shaikh, also, shows that these ill-guided policies stem from the erroneous orthodox 'theory of comparative costs' and he argues that an approach based on the classical theory of 'competitive advantage' is both analytically and empirically superior.

Similarly, Fine (2001a,2001b,2002) criticises the Washington Consensus for consciously neglecting crucial aspects of the development process in order to push the neo-liberal reforms that promote the interests of dominant capitalist economies. He also criticises the post-Washington Consensus for not being a true alternative to its predecessor and for, ultimately sharing the same analytical and policy agenda. Despite its vociferous opposition, it actually shares the same analytical foundations, namely methodological individualism, with the additional flavour of the emphasis on informational asymmetries. This reductionism to individual behaviour, even when supplemented with an emphasis on institutions, cannot grasp the social dimension and moreover class and power relations. Furthermore, despite again Stiglitz's newfound focus on history, it cannot grasp the qualitative dimensions of development and particularly its nature as a transition from one stage of development to another and reduces it to the arrangements required for dealing with market imperfections. Finally, Fine argues that both Consensuses are part of the same 'imperialist' attempt by orthodox economics to colonise fields (such as Economic Development theory), which have hitherto remain no-go areas.

On policy issues, Marxist economists argue that markets, instead of promoting stability and equality, are potential destabilisers and that free competition increases poverty and inequality. This holds especially for financial liberalisation and international capital mobility, which—as the experience of the 1990s reconfirmed—increase domestic financial fragility and trigger balance of payments crises. Additionally, financialisation drains resources that might have fostered the growth of production and employment and increases unproductively the returns of financial intermediaries. Finally, they claim that unbridled competition leads to the concentration and centralisation of capital and, thus, to the creation of national and international monopolies, which impose their interests on the poorer strata and the less developed economies. Ultimately, this process leads to growing divergence between economies, contrary to the orthodox beliefs. In terms of the domestic economy, the Washington Consensus' policies lead to adverse income distribution, since they put the onus on the poorer strata and they systematically erode workers' bargaining power (via greater wage flexibility, reduced regulation and minimum wages). Adverse income distribution worsens even more with privatisations (that make more costly the provision of utilities) and the erosion of the state's redistributive role (through regressive changes in taxation systems and the curtailment of public expenditure).

For the radical critique the way forward for the developing countries is neither the Washington nor the post-Washington Consensus. Instead, another developmental model is required in which the state must have an explicitly active role in promoting trade and industrial policies and positive income redistribution. Moreover, these new state economic functions should be democratically accountable and based on

popular movements. Such an alternative developmental strategy would necessarily have to strive against hegemonical international economic relations.

### **Development as a Social Problem**

In the beginning of the 21<sup>st</sup> century the Washington Consensus is, nominally at least, dead. However, the way forward is far from obvious.

From a long-run point of view the world economy is still living in the aftermath of the 1973 structural crisis. The fact that since then almost all crucial macroeconomic variables exhibit a rather dismal record is tantamount to that. This crisis ended the previous *modus operandi* of capitalism and called for a new architecture of the system. From the perspective of Marxist Political Economy, this was not a simple periodic overaccumulation crisis, but its structural character had to do with the exhaustion of the core elements (relation between paid and unpaid labour time, production and circulation processes, social and political edifice etc.). The first systemic attempt to overcome it followed the prescriptions of the economic orthodoxy of those days, i.e. Keynesianism. Thus, conservative Keynesian policies were employed. Their main feature was that they regarded the crisis simply as an underconsumption one and attempted to solve it via a contradictory reinforcement of demand. In particular, they resorted to austerity measures (where the curtail of any wage increases reduced workers' income and the labour cost and promoted profitability) and state policies (tax cutting, state orders and subsidies) that supported capitalist consumption and the demand between capitalist enterprises. These policies failed, in the long - run, because they weakened intra-capitalist competition, thus deterring the destruction of less competitive capitals.

Then followed the neo-conservative currents, first with their national (monetarism) and then with their internationalised (neo-liberalism) version. Some of their main features were the emphasis on the supply—side, the permission to competition to work unhindered, the withdrawal of the state from the economy and its opening. The withdrawal of the state from economic activities created new spaces for capitalist profitability through privatisations (seldom at basement prices). It curtailed also the ability of the working and popular classes to press for concessions and economic benefits. Together with the liberalisation of internal and external markets, it applied in all markets (including the labour market and for this reason neo-conservatism's attack on workers' position was much more severe than that of conservative Keynesianism) rules of strict competition. These permitted the full application of the clearing force of competition (the survival of the fittest) —with limited ability of the state to adulterate this process - as a means of overcoming the crisis. The Washington Consensus is the brainchild of these currents in the field of Development theory and policy. As such it has similar merits but also suffers from similar deficiencies with its developed countries' blueprints. It has sustained capitalist profitability in the mid—run by providing new areas for investment, reducing labour wage and non—wage costs and clearing the economy from unviable individual capitals. On the other hand, by overemphasising the role of competition it fall to the naïve belief that simply the spontaneous action of individual capitals will suffice to return the capitalist economy to another 'golden era' of accumulation. However, there exist significant contradictions between individual and collective capitalist interests and for this reason the role of the state, as a 'collective capitalist', is necessary. Furthermore, the

width and the depth of the capitalist restructuring required to surpass the structural crisis necessitates much more than the spontaneous action of the market forces. This is another reason why the state is required as a commanding centre, which will guide, motivate and correct the market.

These inabilities lie at the heart of the failures of neo-liberalism and of the Washington Consensus. Tantamount to that is the renewed emphasis – either by its supporters or by its mainstream critics – on the role of institutions. For these reasons both neo-liberalism and the Washington Consensus are virtually dated in the beginning of the 21<sup>st</sup> century and the search began for their successors. Social-liberalist trends appear as such a successor and the post-Washington Consensus is part of them. Their main trust is that they represent a rupture within the continuum of neo-liberalism. They built upon its successes but also strive to correct its deficiencies. Thus a new role for the state-headquarter is researched and also, in the face of serious social upheavals, a more sophisticated form of attacks on and compromises with the working class and the other popular classes.

However, this new emerging orthodoxy has its own deficiencies and, in the cases of the post-Washington Consensus, the radical critique is very accurate on that. In analytical terms, its critique against the Washington Consensus correctly pinpoints its non – social character and its inability to grasp the socio – political dimensions of the development process. However, this defect cannot be repaired by simply adding a role for the state and the institutions to combat market imperfections caused by informational asymmetries and conceived on the basis of methodological individualism. The socio – political dimensions of the development problem are far wider, cannot be grasped properly even by ‘socialised’ versions of

methodological individualism and require more radical and rigorous instruments than simple institution-building. In a sense, where the Washington Consensus creates (or expands) markets—and in some cases where this cannot be done it creates quasi-markets by imposing private-sector modes of operation—the post-Washington Consensus attempts to create quasi-societies as complements to the markets. It neglects that it is social and class interests that create institutional frameworks and rules and sometimes-even markets. The division in different social and class interests is not the result of more, (or less fleeting), informational asymmetries, but of more fundamental and deep-rooted socio-political factors. For all these reasons and despite the valiant critique of its proponent against its predecessor, it seems that the most that the post – Washington Consensus can offer is a compromise with the initial Washington Consensus. This is probably bound to produce similar dismal results with the Washington Consensus regarding the development process. The only area where it may have a limited success is in a form of *gatopardismo*—to borrow from Lucino Visconti’s famous film: everything in the system has to be changed in order for the system to remain unchanged.

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## Neo-Marxist Policies

*Howard J. Sherman*

### **Introduction**

After the death of Marx in 1883, Marxist orthodoxy was first defined by the Socialist parties until the First World War, but after the war the dominant view of Marxism was that of the Soviet Marxists and the Communist International. By contrast, Neo-Marxism may be defined as those Marxists who do not feel bound to any dogma, whether Socialist or Communist, and who are willing to criticize dictatorships calling themselves socialist just as much as they criticize capitalist societies calling themselves democratic. Most neo-Marxists call themselves merely Marxist because they believe that Soviet Marxism distorted Marx, whereas their new Marxism gets back to the spirit of Marx and his main contributions.

### **Global Capitalism**

Neo-Marxists are in favor of a unified global economy, but they are opposed to the present type of pro-corporate global economy. This economy is mainly composed of two kinds of countries. Imperialist countries are defined as those countries who have power over and exploit other countries. Neo-colonial countries are defined as those who are controlled by others and exploited by others. Such an economy has many problems. The most important problems and the Neo-Marxist policies to end them are discussed here. The article concentrates on (1) the problems of globalization and imperialism, (2) the problems of class and inequality, illustrated by data on US capitalism, (3) political and economic democracy, and (4) an equalitarian economic system.

On the global level, the old Marxism said that imperialism is the last stage of capitalism. Neo-Marxists say that

globalization is the present stage of imperialism. Imperialism meant the domination of one country by another for profitable purposes, but globalization means that a relatively few corporations dominate every country in the world. The hundreds of books and articles on globalization do not agree on much, but Neo-Marxists do agree on a few features.

First, these giant corporations extract a large net flow of profit that flows from the less developed countries to the advanced capitalist countries. By “net flow” is meant the amount of profit and interest minus the amount of investment flowing the other way. This net flow from the less developed to the more developed capitalist countries means that the poor, underdeveloped Third World is subsidizing the development of the rich, advanced capitalist countries. This is the reverse of the neo-Marxist policy prescription, which is to end the exploitation of the less developed, neo-colonial countries by the more developed imperialist countries. Only an end to capitalism and its inherently imperialist behavior will allow the replacement of coercion and war by a unified, democratic, global government.

Second, there is vast inequality between countries and within countries. An excellent study of global inequality shows that there has been a very large increase in global inequality in the last two centuries, most of it due to increased inequality between countries (see Francois Bourguignon and Christian Morrisson. 1992). Specifically, the study finds that the Gini coefficient for world inequality of income between individuals has risen from .50 in 1820 to .66 in 1992. In the same period, the share of the top 5 percent of individuals has increased from 32 percent to 36 percent of world income.

Third, Since about the time of the Great Depression, most of the counties of the world have had booms and busts at about the same

time. Globalization ensures that they all go move together, which makes depressions worse than they used to be and much harder to cure. A quantitative study of the cyclical nature of global instability, the misery of unemployment that it generates, and the literature on synchronization is presented in Sherman (1991).

Fourth, in all countries the influence of the giant corporations and vast wealth held by a few distorts democracy, discussed below.

Fifth, the existence of struggles among countries, struggles among corporations, plus inequality and terrible poverty, leads to wars and to wholesale terrorism by governments as well as retail terrorism by oppressed groups. Most penetration and control of the world has been done by peaceful means, but force has also been used. The obvious example is the bloody war in Iraq and Afghanistan waged by the United States and other imperialist countries.

Sixth, the existence of capitalism and greed in every country, especially with rapacious global corporations, leads to environmental devastation – see the excellent Neo-Marxist analysis by John Bellamy Foster, 1994.

Seventh, every capitalist country, developed and underdeveloped, has racial discrimination, both internally and against foreigners – see the excellent Neo-Marxist study by Michael Reich, 1980.

Eighth, every country under global capitalism practices some level of discrimination against women, both because it is profitable for capitalism and because it helps elect reactionary men who support capitalism – see the excellent feminist study by Barbara Sinclair Deckard, 1983.

In each of these eight areas, neo-Marxists support liberal reforms, such as transformation of the United Nations into a democratic world government, laws against

racism, laws against sexism, and laws against environmental destruction. None of the problems, however, can be fully solved unless global capitalism is ended and replaced by a better system, for reasons given in detail below.

## **Definitions**

Orthodox Stalinist Marxism defined socialism to mean government ownership of the economy, but this narrow definition allowed the Soviets to have a government run by dictatorship controlling the economy and the state. Neo-Marxists define socialism as democracy plus equality, both defined below. US leaders and many political scientists define democracy as a procedure to elect representatives and a procedure for free speech – but this narrow definition allows a situation in the United States where there is enormous economic inequality, very limited political democracy, and no economic democracy. Neo-Marxists define democracy to include formal democratic procedures plus effective democracy in the political sphere plus formal procedures and effective democracy in the economic sphere. Effective democracy means a high participation rates and a roughly equal power by everyone to affect the outcome.

## **Capitalism, Democracy and Inequality**

It was said above that all capitalist countries have distorted or restricted democracy. The United states may be used as an example since it's democracy is highly touted by conservatives, but it's limits are constrained by class differences in wealth and power. To understand current US democracy, one must first understand current US economic inequality. Some detail is needed to understand the Neo-Marxist view.

In the United States, at the bottom of the heap are the unemployed and the poorest paid workers, who are about 15 per cent of the

population. The bottom ten percent of the population has no wealth, lives below the poverty line of income, and has heavy debts. The next ten percent up the wealth ladder run from heavy debt to small incomes – an average wealth of \$190 in 1997 (see government data in Chuck Collins, et al, 1999). These are the poorer members of the working class – class is defined as the exploitive relationship between one group and another, such as employees and employers.

Those US workers from the 20<sup>th</sup> percentile to the 60<sup>th</sup> percentile have better wages and have an income at the level that may be called adequate for decency, but no more. They spend their entire income for consumer goods – on the average for bad times and good times – so they save very little on the average. Thus the bottom 60 percent of the US population has negligible wealth. More precisely, the bottom 40 percent have only ½ of one percent of all the wealth. In fact, the bottom 60 percent have only 4.9 percent of all the wealth (Collins 1999:6,9). They work hard to earn enough for adequate survival – but they survive only if you count both woman and man in a two-person family. Without two people working, a large part of these families would be in poverty.

The people from the 60<sup>th</sup> percentile of wealth to the 90<sup>th</sup> percentile of wealth are much better off. The wealth of that comparatively well-off 30 percent of the people is just 22.1 percent of the whole US wealth. So they may be called the highest strata of working class. They are mostly skilled workers, many of the lower-paid professional workers, and many of the lower paid managerial workers.

Near the top, those from the 90<sup>th</sup> percentile to the 99<sup>th</sup> percentile have 34.1 percent of all the wealth (Collins 1999:9). They include highly paid professional workers, highly paid managerial workers, and

many small and medium size business owners. They may be called the upper middle class or the top strata of the working class.

Last, but not least, are the top dogs are the top one percent of wealth owners, the rich and super-rich. They own 40.1 percent of the wealth. In 1997, their wealth ranged from \$2,419,000 to 100 billion dollars (Collins 1999:9). Most of their income comes from stocks and bonds and rents -- so they may be called the capitalist class. Many of them do work as managers, who are paid millions a year for their work – but most managers own a significant part of their company, so they have a big say in how much they are paid – thus their pay usually exceeds the market value of their “work.” In fact, the latest survey shows that Corporate Executive Officers averaged 500 times the income of the average worker!

Some orthodox economists claim that there is at least equality of opportunity, but most people with wealth have inherited significant wealth. Also, there is discrimination by race and gender – so the playing field is not level.

Some orthodox economists claim that at least things are getting better and better as time goes on. But in dollars of constant purchasing power, the average weekly wage went from \$502 in 1973 to \$442 in 1998 (Collins 1999:28). At the same time as that decline in the weekly wage, production rose by 32.7 percent (p.28). Since wages by a large percent, while production rose by a large percent, it follows that profits rose greatly.

Supposedly, there is a safety net under workers, but the legally established minimum wage has declined by 37 percent since 1960. So things have not gotten better for most people in the US economy. During the whole boom of the 1990s, corporate profits rose by over 50 percent and the stock market rose by over 100 percent, so some of the super rich

became much richer. The wealth of many in the upper middle class did expand rapidly during the boom and stock market bubble of the late 1990s, but then the bubble burst and trillions of dollars were lost in the stock market, with many small investors losing much of their retirement savings.

### **Affect of Inequality on Democracy**

As an example of democracy under global capitalism, US democracy has three problems. First, its procedures need improvement, including lost votes and a system where someone can win with far less than a majority – or even less than the loser in the case of President Bush. Second, even with perfect procedures, there is still the fact that elections are decided by money. In 2000, the two major parties spent three billion dollars on their candidates, while political action committees also spent a huge sum. Furthermore, only half the eligible voters voted in 2000 and only about a third in 2002. Those who did not vote were mainly people with lower incomes, who received their income from labor. Thus the elections are controlled by those with money and politicians need not worry about the wishes of most of the working class because most of the working class does not vote.

Third, even if there were perfect procedures, no advantage to wealth, and high participation rates, the United States would still be far from a high level of democracy. Democracy includes economic democracy, but there is zero economic democracy in the United States. Only the major owners of corporations decide who runs the corporations, consequently who is hired and fired, how much they are paid, what is produced, what are the safety regulations, and so forth. Ordinary workers, who are most of the population, only take orders, they do not participate in decision-making or in profits.

### **Neo-Marxist Policies on Democracy**

The United Nations and each country need fully democratic procedures. See discussion of the necessary mechanisms for democracy in future, non-capitalist societies in Miliband, 1994.

An obvious political reform, supported by Neo-Marxists in all capitalist countries, is to prohibit all private contributions and use public financing of candidates in all elections. This will still not prevent wealth from ruling elections in many other ways. Therefore, it is necessary to prevent vast inequality in the society. Only a society with a high degree of equality can have a truly effective political democracy -- with equal access to funds, to the media, and so forth. Equality requires both economic democracy and direct measures for equality.

### **Neo-Marxist Policy for Economic Democracy**

Economic democracy is important for its own sake, but it is also a vital underpinning for political democracy. There are two basic modes of economic democracy possible, each with many subcategories. One way is to have governmental control of the economy – at local, state, and federal levels – with democratic control of the government. Another form of democratic control is control by the workers in each enterprise. Control by the government implies coordination through non-market planning. Control by the workers in an enterprise implies coordination through the market mechanism.

Although utopians speak as if other forms were possible, these are the only two possibilities recognized as viable by Neo-Marxists. Of course, there can be a mixed system, including both forms. Thus, some industries or size categories of firms should be run by one system of coordination and some by the other. Also within government-

run firms, some functions can be done by the democratic will of the workers, while other are done by the democratically appointed manager for the government. In worker-run firms, in addition to democratic control by the workers, there should be government controls of some functions, for example, environmental regulations.

Both the market and the government planning mechanism have advantages and disadvantages. These comparisons of market versus plan are discussed in detail in Schweikart et al (1998). Briefly, government planning can ensure full employment of all resources. Resources were fully used in the Soviet Union, even under an inefficient dictatorship. Democratic central planning also has the problem of enormous information flow and computational burden, so that is a source of inefficiency. The Soviet case is only suggestive as to the merits or demerits of planning because it was dictatorial, not democratic. It does suggest, however, that any central planning is likely to have a high degree of employment of all resources, but a problem with efficient use of resources.

The market system of global capitalism is also only suggestive of the merits and demerits of the market because it is under capitalism, not under democratic socialism. It tends to generate enormous instability, recession, depression, and uncertainty at all times, with misery at the worst times, with unemployment for workers and loss of savings for middle class investors in the stock market. On the other hand, the capitalist market is good at providing anything desired to those with plenty of money.

So there is evidence, but not definitive evidence, that democratic government planning would mean full employment and significant inefficiency. But the evidence also indicates the democratic market socialism would mean efficient provision of goods to

those with money, but a high degree of unemployment and instability. Of course, this is speculation because there has been no large and long-lived example of either type of democratic socialism. Either would be far more democratic than the present system, both in the political sphere and the economic sphere.

### **Neo-Marxist Policies for Equality**

The Neo-Marxist view of socialism includes both political and economic democracy, as discussed above, and measures for equality. Progressive taxation and welfare spending ameliorate, but do not change the capitalist system. Neo-Marxists will fight for all reforms benefiting most people, but a high degree of equality is impossible to achieve in a capitalist system for many reasons. For one thing, job discipline depends on the threat of unemployment and/or low wages. Any movement strong enough to change the basic inequality of capitalism is likely to consider systemic change rather than reform under capitalism.

A democratic socialist society would move toward far more equality by two radical means. As discussed above, most of the economy would be taken over by worker-led firms and by local, state and federal government. Democratic ownership by workers and/or the public would prevent most private profits, the largest source of inequality. Second, a democratic socialist society would move toward an expansion of free goods and services – where “free” means free to the final consumer, no matter how its is produced (and the term “goods” will mean goods and services hereafter).

Some utopian socialists believed that it was possible to achieve immediately a society in which all goods and services would be free. While criticizing utopians for unrealistic expectations, many Neo-Marxists have continued to have a vision that

eventually in the distant future all goods and services would be free.

At the other extreme, conservatives ridicule any free good as an impossible Free Lunch produced with no work. Conservatives have also presented three serious arguments against provision of goods produced by labor at a zero price.

First, if all goods are free, there will be no incentives to work. Thus there will be a rapid decline in production. Second, if all goods are free, consumers will want unlimited amounts. Thus, there will be an enormous jump in demand without enough supply to meet the demand. Third, if all goods are free, the lack of prices means that there can be no rational planning. Thus, the economy will be chaotic and totally inefficient.

There is a vast conservative literature on these subjects, but the most serious and comprehensive critique of the Marxist view of universal free goods is given in Peter Wiles (1962), written during the height of Soviet discussions of socialism and communism. Wiles provides every known citation to Marx and Engel's on this subject, followed by a vast number of references to all of the conservative arguments, ranging from famous ones like those of Hayek and Friedman to obscure ones. All the objections focus on lack of incentives, demand problems and planning problems. Wiles' book is thus the best single source for the conservative views stated here (see also the Marxist reply to Wiles in Sherman 1970).

Each of the three conservative arguments is valid in the extreme case of a shift overnight from a capitalist price system to a type of socialism with all free goods. This does not answer the question, however, as to whether it is realistic to introduce free goods slowly into a democratic socialist society. It should be noted that even in the present advanced capitalist economies there are many

free goods, from schools and parks to police and armies—so the question is not yes or no, but the extent of free goods. The fact that present capitalist economies do have some free goods that cause no problems of incentives or planning shows that the conservative arguments are greatly overstated.

Suppose a democratic socialist society introduced one or two more free goods, such as universal health care and universal higher education. It is hard to see how health and education could have any negative effect on incentives to work. People would still need food, clothing and shelter—and would still want many luxuries. So there would be no harmful affect on incentives. In fact, higher education may increase incentives to do some kinds of work.

After health care and education, a guarantee of minimum food for everyone – perhaps by universal food stamps – would be high on the list. Many studies have shown that, instead of millions of people starving to death, it is perfectly possible at our present level of technology to deliver adequate food to everyone on earth—it is only human institutions that prevent it (see e.g., A. K. Sen, 1980, or Keith Griffin, 1987).

If still more free goods were gradually added over many years – such as minimum food by universal food stamps – incentives might be affected at some point under present psychology. No further free goods could then be added, unless psychology changed due to new experiences as well as new education and new media. Or unless society decided to accept somewhat lower incentives for the sake of the good effects on equality and productivity from free goods, such as health care, education, or cheaper public transport.

The conservative objection about excess demand can be answered with precision for each free good added to the list. If a good is a luxury, such as palaces or yachts, then people

may have an almost infinite capacity to use more of them if the price is zero. So luxuries cannot be made free under any conceivable psychology and technology known to us. But the situation is different for necessities, such as health care. The amount of health care necessary for everyone at a high standard can be estimated fairly exactly, using the usual actuarial techniques of the insurance companies. Doctors would have the right to deny excessive health care to hypochondriacs, as is the case in most insurance schemes at present. Similarly, one can estimate higher education needs or even needs for minimum food at some reasonable standard. Thus, a democratic socialist society would never introduce a new free good unless it had the resources to meet the estimated demand. Moreover, technology has made it possible to perform miracles, even though the fruits of these miracles have so far been largely restricted to the rich.

If all goods are free and non-market, then there are no market prices to guide planning in an efficient way – though this problem might be overcome by enough information and enough computer space. But if the proposal is only to add one more free good, such as a new city park, then this argument is silly. Since the prices of all inputs would still be on the market, there is no problem in pricing information to avoid inefficiency. Even a health system for a whole country can easily be priced and run efficiently, since free prices to patients does not abolish the known prices of doctors and equipment.

In terms of strategy, it is important to stress that, whether under capitalism or socialism, a good, such as health care, must never be given only to the poor, but must always be universal. Of course, there are all the usual reasons for universality: taking it out of the alienating market context completely, making absolutely sure that everyone has it, increasing equality for the

whole middle income group as well as the poor, and giving certainty to everyone. But there is also the important tactical consideration that a program for only a small minority will never be popular; whereas a program for all will have enormous support and cannot be removed once it is in place without enormous conflict.

In the Neo-Marxist view, the struggle for free goods must avoid two erroneous extremes. One extreme claims that it is possible to jump to utopia, that is, to immediate complete provision of free goods and transformation to a higher level of human functioning without material incentive. On the other hand, Neo-Marxists also reject the concept that all that is necessary are reforms so minor and so gradual, over many decades or centuries, that the capitalist class and its political representatives will accept them without a fight—but no such harmonious path is possible. Instead a tough struggle will be necessary to achieve a significant level of free goods in a democratic socialist society.

In the old Soviet Union many Marxist writers argued that there is inevitable progression from capitalism, to socialism to a communist utopia in which all goods are free (see for example, Klein, 1961). Neo-Marxists have not only objected to any notion of inevitability. They have also noted that under present and conceivable technology and psychology it would be impossible to run an economy with all goods being free. Of course, science fiction utopias are very important to motivate radicals (see Williamson 1997).

## Conclusions

The Neo-Marxist literature finds that it is possible to have political and economic democracy with a high degree of equality, but only with a lengthy struggle on many issues. First, for Neo-Marxist debates on global policy, see the journals: Historical



Materialism, Monthly Review, New Left Review, and Review of Radical Political Economy. Among the many recent books and articles by Neo-Marxists on globalization and imperialism, the most outstanding are the works by Foster (2006), Hahnel (2005), O'Hara (2004), and Pollin (2004).

Second, political democracy must be not just formal, but effective for all groups. Political democracy is restricted by class differences in power and wealth.

We showed that there is vast inequality in wealth in the United States. The capitalist owners of corporations have vast sums of money that can be used to influence political parties, the media, and the voters. To end the influence of wealth on government and elections requires economic democracy and policies for equality.

Third, economic democracy can be in the form of public ownership by a democratic representative body. Economic democracy can also be through the form of cooperative employee's ownership. Or a mixture of the two.

Fourth, equality can be increased by democratic ownership, but also by free goods provided by the public in some important areas, such as health and education.

Fifth, racism, sexism, booms and busts, and environmental destruction can be reduced by reforms inside of capitalism, but can be abolished only under economic democracy.

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## North American Politics and Policies

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North American democracies differ from other advanced industrial democracies in many ways. Two particular factors that have influenced the structure of government, political parties and policies in Canada, Greenland, the United Mexican States, and the United States of America, are their relative isolation from the rest of the world and the fact that each was a settler society. As an island, Greenland is the most isolated. Its nearest neighbor is Canada. Along with its proximity to Greenland, Canada shares borders with the United States and no other countries. The United States shares borders with Canada and Mexico. Mexico shares borders with the United States, Guatemala, and Belize. Together, the geographic isolation of these countries has meant they did not have to maintain complicated foreign relations with a large number of countries during their formative years. This is not to say that these countries did not interact with other countries. In fact, there has been significant interaction between Canada, the United States, and Mexico over time. Greenland's independence came much later than it did for the other three, but its remote location and harsh environment contributed to its isolation.

All four countries have a democratic form of government now and the transition to this form may have ironically been made easier by the fact that, as colonies, none of these countries had a monarch on their soil to depose. They had no long-entrenched form of government to overthrow or overcome. Each also had legitimate complaints about a distant and unresponsive colonial government. The long distances between the colonies and the seats of power meant that the colonies developed a certain amount of autonomy and

a sense of self-governance. Also, these colonies had to deal with indigenous people and that has shaped internal policy and foreign relations. While there are striking similarities in the formation of each of these countries, there are significant differences between them concerning the form of government, foreign and defense policies, and economic conditions.

The similar beginnings of these four countries have produced four democracies, but two different democratic systems. Mexico and the United States each have presidential democracies while Canada and Greenland have parliamentary democracies. These differences are important in terms of the ease with which policies can be adopted and implemented. The parliamentary system merges the executive and legislative branches in a way that provides for a more unified system that is generally more successful at advancing a policy agenda. Canada has provided many examples of this. There are exceptions to this rule. If it is a coalition of parties that has formed the government, it is less likely to be successful. Greenland has provided examples of this. In the presidential system there are checks and balances between the executive and legislative branches, but the separation of the powers can make it more difficult to advance a policy agenda. When the legislative and executive branches are controlled by the same political party, policy victories are more likely. Until recently, Mexico, with its one-party dominance, had been a good example of the advantages of a unified government in a presidential system. At various points in time, the United States has provided good examples as well.

Another large difference among these nations is the relative attention paid to their defense posture, particularly the United States' massive military and military spending as a world superpower, including over 144 million people available to serve

(2008 estimate) and over four percent of the country's gross domestic product (GDP) spent on the military (2005 estimate) (CIA World Factbook 2008). Greenland has fewer than 16,000 people available for military service (2008 estimate) and does not have a regulated military. It receives its military protection from Denmark. Mexico spends one of the smallest percentages of its GDP (0.5%) on its military (2006 estimate) among countries spending any money on military and has over 57 million people available for military service (2008 estimate). Canada spends just over one percent of its GDP on the military (2005 estimate) and has fewer than 16 million people available for military service (2008 estimate).

The United States has the largest GDP (purchasing power parity) in the world at 13.86 trillion dollars (2007 estimate) (CIA World Factbook 2008). Canada and Mexico have GDPs over one trillion dollars (2007 estimates: Canada, \$1.274 trillion; Mexico, \$1.353 trillion) and Greenland's GDP is just over one billion dollars (2001 estimate). Size is not the only thing separating the economies of these countries. Canada and the United States are large, affluent, high-tech industrial societies with diverse economies. Mexico has a large economy with some modern industries, but also has many developing and/or underdeveloped industries. It is an economy that is moving from significant government control to being dominated more and more by the private sector. Greenland has a very limited economy that relies heavily on fishing and subsidies from Denmark. Canada and Mexico do significant trading with the United States. Over three quarters of Canada's exports go into the United States. Trade between Mexico and the United States has tripled since the implementation of the North American Free Trade Agreement (NAFTA) in 1994. This also explains why relations with the United States plays such a

large role in domestic policy debates in these countries. Canada is the only one of these countries that does not have a trade deficit.

The similarities and differences among these nations of North America greatly influence how political parties function. These nations' party systems tend to be distinctive compared to other advanced industrial democracies in that parties have not necessarily been mechanisms of democratization and have tended to be more ideologically pragmatic. Parties play a central role in policy formation, but few scholars would confuse the policymaking process with the party government model found in most West European democracies, where party manifestoes clarify ultimate policy direction and elected party members demonstrate unwavering loyalty to their parties' positions. Party scholars have long debated how best to conceive of the role of parties in North American democracies and ultimately the goals of these parties. In particular, scholars struggle over whether American parties in particular view electoral success as simply a means to achieving ideological policy ends, or whether parties, in order to avoid upsetting voters with ideological extremity in government policy, choose to mediate their policy goals and equate success strictly with winning elections. Consequently, different definitions of political parties have been produced. Some define parties as institutions primarily focusing on elections (see Downs, 1957; Schlesinger, 1985), while others define parties more as institutions pursuing policy goals (Lipset & Rokkan 1967:5, Klingemann et al. 1994:5). In reality, none of these approaches fully segregates these goals from each other. Party experts recognize that parties consider both of these concerns. Indeed, some theorists differentiate party activities based on the numerous functions parties must fulfill (see Key 1964), or classify the nature of party systems around the

number of parties, or their relative pragmatism vs. ideology, etc. (see Sartori 1976 for a broader discussion of these issues). Even given the nuanced definitions and classifications scholars have adopted to deal with the complexities of political parties in democracies, most scholars have generally agreed that the party systems of the major North American countries are not as ideological or programmatic as are party systems in other advanced industrial democracies.

There are different reasons provided for the lack of strong policy-based parties in North America. Many point to the limited number of competitive parties as a reason for the avoidance of ideological partisan appeals. Following Downs' (1957) classic study of the distribution of party competition, the conventional wisdom has followed that in two-party systems it is best to appeal to the median voter rather than to ideologically extreme voters. Other democracies, whose institutions welcome more parties, allow these parties to be both competitive and ideological and, as a result, broaden the range of ideological competition. Therefore, for many scholars the number of parties in the United States and Mexico and, to an extent Canada, explains why competition has been more pragmatic than ideological.

Explanations of social cleavage-based party formation and party development also provide important insight into why North American parties have not typically been thought to be as ideological as their counterparts in Europe. Lipset and Rokkan's (1967) classic work on European party formation argues that the key component in the development of political parties stemmed from social cleavages arising from the National and Industrial Revolutions. Further, Lipset and Rokkan argue that the promotion of the right to vote among the social groupings that formed from these

revolutionary movements further unified these eventual parties. Thus, these social groups' loyalty to their party came from both the articulation of a social group's interests and the ultimate provision of political power, which further cemented the loyalty of these social groups with their party. North American parties have typically not been based on such deep social divisions and have had the main cleavage of competition change at numerous times in their history. Further, broad voting rights, particularly in the United States and Canada, removed the fight for suffrage as a source of affection for parties as well.

The more pragmatic approach of the political parties in Canada, the United States, and Mexico have provided these nations with less ideological rigidity in policymaking, though critics might say these catch-all parties do not sufficiently stand for anything. However a person perceives these parties as operating, they do not enjoy great affinity with their relative public. The World Values Survey asks respondents for the degree of confidence that they have in political parties. In 1999 (USA) and 2000 (Canada and Mexico), over 75 percent of the respondents had no or not very much confidence in political parties. The percentage in Mexico increased five points from 1990 to 2000. Mexican respondents were much more pessimistic than Canadian or United States respondents. Almost 40 percent of the Mexican respondents had no confidence in political parties while less than 20 percent of the respondents from Canada or the United States had that opinion.

It is important to keep in mind, however, that the party systems of Canada, Mexico, and the United States not only differ significantly from party systems of other democracies—especially those in western Europe—but these party systems are also quite distinct from one another as well.

Consequently, classifying these political parties, much less understanding their functions as political parties compared to other countries, is challenging. Specific elements of each nation's party system development and history also explain the pragmatism of these parties in pursuit of electoral success and public policy, but also how political parties eventually bring about public policy.

Historically scholars have tended to view American and Canadian parties as more pragmatic than programmatic, and correctly viewed the Mexican party system as so uncompetitive as to border on undemocratic. Ironically, as European parties have adopted more pragmatism for the sake of electoral competition by easing some of their ideological appeals, in some ways North American parties have illustrated the opposite trend.

## **Canada**

Canada considers July 1, 1867, to be its independence day. This is the day that the Canadian Parliament came into being. The four original provinces were New Brunswick, Nova Scotia, Ontario, and Quebec. Manitoba (1870), British Columbia (1871), Prince Edward Island (1873), Alberta (1905), Saskatchewan (1905), and Newfoundland (1949) brought the number of provinces to ten. There also are three territories—Northwest Territory, Nunavut, and Yukon.

In 1931, Canada was recognized as an autonomous state within the British Commonwealth and on April 17, 1982, the British North America Act (1867) was replaced by the Act of Canada, which gave Canada the ability to reform its constitution.

Canada is a democratic constitutional monarchy with a bicameral parliament. The British monarch (Queen Elizabeth II) is also the Canadian monarch and is represented in

Canada by the Governor General (Michaëlle Jean, 27<sup>th</sup> Governor General of Canada). Members of the Senate are appointed by the Governor General on the advice of the Prime Minister. Originally senators were appointed for life, but in 1965 a constitutional amendment introduced a retirement age of 75. Members of the House of Commons are elected directly from single-member districts (ridings). The constitution provides that the House of Commons may meet for no longer than five years. Parliament can be dissolved before the five-year term expires. Officially, it is the governor general who dissolves Parliament, but it is normally done only on the advice of the prime minister. Dissolution of Parliament does not effect the composition of the Senate, but it does create the need for elections of members of the House of Commons and, therefore, the Prime Minister.

The heterogeneity of Canadian society does not lend itself to large cohesive partisan groupings based on cleavages. Early partisan divisions grew from debates over the proper relative political power that should be given locally to the Canadian colonies versus England (Wearing 1996). Further, because of the complex social and cultural divisions among the provinces, no clear line of party competition could develop nationally (Kornberg et al 1992). As mentioned above, in Canada the right to vote was always much more broadly available than in Europe, even though by no means did the franchise reach everyone. Together this meant that tight connection between parties and social groupings (save French-speaking Quebec) did not form in Canada. Indeed, Lipset and Rokkan refer to Canada as “deviant” in their lack of strong, working-class parties, for example, because of their “early enfranchisement, high mobility, entrenched federalism, and marked regional, ethnic and religious diversity” (1967:31).

Significant regional differences exist in Canada because of less well-developed national parties. Often these regional distinctions take the form of antipathy toward the political power of other regions. First, the question of whether Quebec should be considered a distinct province of Canada has long been debated and drove the intense Meech Lake Accord debates. While many French-Canadians push for this distinction, other regions resent this. Further, the enormous political clout of Ontario as a province and Ottawa as a capital has not always set well with the Maritime eastern coastal provinces nor the western provinces. A mid-twentieth century populism and a subsequent feeling that western extractive resources like oil and mining were benefiting eastern industry at the expense of western provincial profits meant that regionalism has often outweighed other political divisions in the stances parties have taken.

Canada has two major parties, but other parties clearly influence politics significantly in this federal system. While the Conservative and Liberal parties have formed the ruling government of Canada for more than 80 years, other parties have found success at the provincial level. For example, in June of 2003, Gary Doer of the New Democratic Party was reelected to a second term as the Premier of Manitoba with an increased majority in the Provincial Legislature. Dennis Fentie is the Premier of Yukon and a member of the Yukon Party. Lorne Calvert is the Premier of Saskatchewan and a member of the New Democratic Party. From 1994 to 2003, the premiers of Quebec were members of the Parti Quebecois. Additionally, the regional distinctions and distribution of the population in Canada has made it possible for regional political parties to influence national politics. In 2005, approximately 62 percent of the Canadian population lived in Ontario (38.9%) and Quebec (23.5%). This helps to

explain how a regional political party like the Bloc Quebecois can win 51 of 308 seats in the Canadian House of Commons.

A review of control of the House of Commons shows that over its 139-year history, five political parties have formed the government. A review of prime ministers shows that six political parties have named the prime minister. Both of these numbers are misleading because there really have been only two political parties in control. Those two parties are the Liberal Party of Canada and the Conservative Party of Canada (under different names). While the parties historically have been stable, they have had low moments. In particular, the Conservative Party lost its parliamentary majority and retained only two seats (of 295) in an electoral bloodbath in 1993. This has led to significant changes within the party and demonstrated that major issues in Canadian politics may tend not to be ideological and can threaten even the strongest parties.

Though the Conservative Party of Canada does not entirely match the classic liberal components of the American Republican Party, and the Liberal Party positions itself much more as a classic liberal party than the American Democratic Party, neither are particularly ideological (Schwartz, 1974; Lipset and Rokkan 1967). The strong regional nature of the country also takes from the development of unified parties. Parties often behave differently at the regional level than they do at the federal level (Schwartz, 1974). Further, in recent decades issues like provincial autonomy and trade relations with the United States have driven the political debate and election results. This makes classifying Canadian parties very difficult.

#### *Conservative Party of Canada*

On the surface, the Conservative Party of Canada (CPC) appears to be a new political party. However, the CPC is actually a

combination of two established political parties. After merging with the Canadian Alliance (formerly the Reform Party of Canada) that championed western provincial interests in 2003, the Progressive Conservatives became the Conservative Party of Canada, and won its first seats in the 2004 election. In that election they won 99 seats, enough to be the Official Opposition Caucus.

In the 20<sup>th</sup> Century, conservative parties controlled the government for approximately 30 years. The CPC was created in 2003 when Stephen Harper, leader of the Canadian Alliance, and Peter MacKay, leader of the Progressive Conservative Party, brought the two parties together. Their goal was to create a national conservative party that could challenge the Liberal Party of Canada (LPC) for control of the government. It did not take long for the CPC to become the governing party. In 2006, the CPC moved from 99 to 124 seats and the LPC fell from 136 to 103 seats.

At the time of the 2006 elections, the CPC was led by Stephen Harper. Harper is from the former Reform Party wing of the party. The CPC had a two-pronged approach to the campaign. The first was to challenge the accuracy and interpretation of the claims of successes made by the LPC. The second was to call for government to be more accountable and responsive to the needs of the people of Canada. Specifically, the CPC pledged to reduce the Goods and Services Tax (GST) and eliminate certain capital gains tax. They called for limiting the growth of some government programs to the rate of inflation. They also pledged to introduce mandatory minimum sentences for certain crimes and to hold a vote to restore the traditional definition of marriage.

#### *Liberal Party of Canada*

The Liberal Party of Canada (LPC) is the only party remaining from 1867. Over the

years it has seen times of great power and near elimination. For example during the 18<sup>th</sup> Parliament (1935-1940) and 19<sup>th</sup> Parliament (1940-1945), it held 70 percent of the seats in the House of Commons. However during the 13<sup>th</sup> Parliament (1917-1921) it held less than two percent of the seats. In the 32<sup>nd</sup> Parliament (1980-1984) it held 51 percent of the seats and in the 33<sup>rd</sup> Parliament (1984-1988) it held only 14 percent. Currently it holds 33 percent of the seats, having lost control of Parliament in 2006.

It typically has been viewed as a centrist party balancing itself between the left and the right. The LPC is often given credit for implementing many of the Canadian social welfare programs that were put in place during the 1900s and the promotion of multiculturalism. It should be noted that the eagerness with which some of this work was done was, at times, less than overwhelming.

At the time of the 2006 elections, the LPC was the governing party led by Paul Martin. They campaigned on a platform intended to demonstrate a centrist tendency. They referred to eight consecutive budget surpluses and a \$63 billion reduction in the national debt to tout their fiscally responsible nature. The platform also publicized the creation of a \$5.5 billion *Wait Times Reduction Fund* to hire more health professionals and guaranteed health transfers to provinces to grow by six percent each year for the next 10 years. Increased income support for seniors was also presented as a success for the LPC.

#### *Bloc Quebecois Party*

For decades there have been divisions among Canadians over language and culture. The manifestation of this in political parties can be seen in the Bloc Quebecois (BQ). This francophone group was organized by Lucien Bouchard and others after the failure of the Meech Lake Accord in the mid-1990s. Even though the BQ fielded candidates only in the



province of Quebec, they scored an impressive victory in 1993 when they took 55 seats and became the official opposition party.

At the time of the 2006 elections, the BQ was led by Gilles Duceppe. They have not matched that high-water mark of 55 seats won in 1993, but they do have 51 of the 75 seats from Quebec in the Canadian Parliament. While it is not possible for the BQ to win a majority of seats in the parliament by winning every seat from Quebec, it does demonstrate how close a regional political party (especially one from Quebec or Ontario) could be to becoming the governing party.

Although the BQ has positions on many of the issues discussed by most parties such as the Goods and Services Tax, transfers from the federal government to the provinces, accessibility to health care, and foreign affairs, the issues typically are discussed in terms of how they relate to Quebec, the people of Quebec, and the pursuit of sovereignty for Quebec.

#### *New Democratic Party*

The New Democratic Party (NDP) is a social-democratic party that was formed in 1961 when the Canadian Labour Congress and the Cooperative Commonwealth Federation merged. It has never achieved the success of the Bloc Quebecois (BQ) in terms of its position in the federal government. However, from 1965 to 1993 it was the third largest party in Parliament. It also has a broader geographic appeal than the BQ. At various times during the 1990s, the NDP served as the governing party in Ontario, British Columbia, and Saskatchewan.

Traditionally, the NDP has supported and pursued broader social benefits, a planned economy, and internationalist foreign policy. In 2006, under the leadership of Jack Layton, the NDP continued those positions. They

campaigns on better in-home care for seniors, an increase in child benefit payments to low-income families, improved access to education and skills training, help for high-cost prescription drugs, and training more nurses and doctors in order to cut waiting lists.

#### *Other Parties*

While the Conservative Party of Canada, the Liberal Party of Canada, the Bloc Quebecois, and the New Democratic Party are the dominate parties in Canada, there are several other parties that are still active. The other registered political parties are the Animal Alliance Environment Voters Party of Canada, Canadian Action Party, Christian Heritage Party of Canada, Communist Party of Canada, First Peoples National Party of Canada, Green Party of Canada, Libertarian Party of Canada, Marijuana Party, Marxist-Leninist Party of Canada, Progressive Canadian Party, and the Western Block Party.

#### **Greenland**

Danish colonization of Greenland, the world's largest island and second largest tract of frozen land, began in the 18<sup>th</sup> Century. Later that century, Denmark assumed a monopoly on trade with Greenland. During World War II, the United States assumed protective custody of Greenland. As a result of the North Atlantic Treaty, Denmark and the United States entered into an agreement to build a military base in Thule, Greenland. In 1953, Greenland became a county of Denmark on equal terms with other Danish counties. On May 1, 1979, Greenland gained home-rule authority thanks to a referendum vote held on January 1, 1979.

Greenland is an autonomous Danish province with a unicameral parliament (Landsting) led by a premier. Queen Margrethe II is the Danish Monarch. The chief representative of the Danish

government in Greenland is the High Commissioner (Soren Hald Moller). This position serves as the liaison between the Danish and home rule authorities. The first parliamentary elections were held on April 6, 1979. The first parliament had 21 seats. The number of seats has expanded to 31. Each parliament is elected for a four-year term, but the premier can call for elections to be held early. Seats in the parliament are distributed based on the d'Hondt's proportional method. There had been eight constituencies, but, as of the 1999 election, there is only one constituency. Greenlanders also elect two members to the Danish Parliament (Folketing) and have one representative on the Nordic Council.

The first Greenlandic political party, a nationalist Inuit party, was formed in 1964. The largest political party in Greenland, Siumut (Forward) party, was formed in 1977 as a continuation of the Sujumut movement, which was formed in 1971. Although many issues contributed to the push for autonomy, four are considered to be integral. The first was the construction of the military base in Thule resulting in the displacement of Inuit people. The second came in 1968 when a United States B-52 carrying nuclear weapons, in violation of the Danish ban on nuclear weapons on its territory, crashed near the Thule base. The third came in 1973 when Greenland was forced to join the European Economic Community (EEC) in spite of its perceived closer connection to North American countries. The fourth came in 1974 when the Danish government made concessions to multinational corporations for oil exploration in fishing grounds off the west coast of Greenland.

Five issues have driven politics in Greenland since it achieved home-rule authority. The first is greater independence from Denmark including more influence in foreign affairs. The second is what has been

characterized as an accelerated transition away from its traditional way of life to a modern industrial welfare state. The third is its economic dependence on fishing and changes in the most bountiful fishing grounds. The fourth is a collection of social issues that include a housing shortage, inadequate healthcare and education systems, and alcohol and drug abuse. The fifth issue is accusations of corruption and cronyism.

Unlike Canada and the United States, Greenland does have clearly defined social cleavages. According to the International Work Group for Indigenous Affairs, approximately 88 percent of the 56,900 people living in Greenland are indigenous. The majority of the remaining 12 percent are from Denmark. The indigenous people have led the fight for independence from Denmark as well as preservation of their culture and programs for indigenous people. Contributing to the cleavage is the belief among the Inuit that a disproportionate percentage of the positions in the government are held by people from Denmark. In spite of this cleavage, and the significant population advantage, the Inuit Party has never been the governing party. At best it has been part of a coalition government formed by another party.

Another difference between Greenland and the other North American countries is that some of the Greenlandic political parties have very definite ties to political parties in Europe (specifically in Denmark). This has meant parties that are more ideological than those found in Canada and the United States. In spite of the more ideological nature of some Greenlandic parties, the moderate party (Siumut) is the only party that has ever governed and it has done so by forming coalitions with one or more ideological parties.

*Siumut (Forward)*

Over the 27 years of home rule, the ruling government of Greenland has been formed by the Siumut by itself or by a coalition including the Siumut. The premier has always been a Siumut. Jonathan Motzfeldt was the first premier and served more years in that capacity than either of the other two men to serve as premier.

There have been nine parliamentary elections in Greenland. In seven of them, the Siumut received the largest percentage of votes. In the two elections when they did not receive the largest percentage of votes (1983 and 1987), they were able to form a coalition with another party (Inuit Ataqatigiit) to remain the ruling party.

Siumut is a social democrat party that has championed a more diacritic Greenlandic identity and pushed for increasing autonomy from Denmark, often times stopping short of a call for complete independence. It also was instrumental in Greenland leaving the EEC. Leading up to the 2005 election, Siumut helped push through a reform of the way Greenlanders paid for electricity. The result of the reform was that no longer would the price of electricity be the same for every rate payer regardless of the price to produce and deliver the electricity to the rate payer. Additionally, it was assumed that Siumut would have trouble forming a coalition government because of fundamental differences with other parties, or because of recent significant disagreements. In fact, the Demokratiit and the Inuit parties campaigned on replacing the Siumut, but failed to do so. In 2005, Siumut managed to hold on to 10 of 31 seats and formed a coalition government with the Inuit Ataqatigiit and the Atassut Party.

#### *Atassut (Solidarity or The Link) Party*

The Atassut Party began as a movement in 1978 and officially became a political party in 1981. It has been the main opposition party

since home-rule authority was granted to Greenland. In 1983 and 1987, the Atassut Party won the largest percentage of votes in the parliamentary elections. In spite of its plurality of seats in the parliament, it failed to form a coalition government in either year.

The Atassut Party is aligned with the Venstre in Denmark. While the Atassut Party favors home rule, it does not believe in complete independence for Greenland. Instead, it believes in the interdependence of Greenland and Denmark. It supported Greenland remaining in the EEC and rejoining the EEC and European Union (EU) in order to receive subsidies. Traditionally it has supported greater privatization of commerce. While the Atassut Party has often been a part of the ruling coalition, the coalitions have broken up over differences regarding independence, economic policy, and the budget. After the 2005 election, the Atassut Party became a minority partner in the coalition government, but it has seen a gradual decrease in its number of seats in the parliament. They currently have six of 31 seats.

#### *Inuit Ataqatigiit (Inuit Brotherhood) Party*

The Inuit Ataqatigiit (IA) was founded in 1978 and has seen an increase in support. Although it has never received the largest percentage of votes, it has been part of coalition governments as far back as 1983 when its two seats were enough to form a majority coalition with the Siumut. The support for IA in 1983 came from younger radical Siumut members.

IA is the most pro-independence party in Greenland calling for complete independence from Denmark. They have called for Greenland citizenship to be limited to people of Inuit parentage as part of their plan to preserve the Inuit culture. Additionally, they favor a progressive tax structure and more emphasis on environmental protection. It has

formed coalition governments with the Siumut many times, often finding common ground on issues such as complete control of mineral resources or increasing independence. In many instances, the agreement between the two parties has disappeared when Siumut has not been willing to back the positions of Inuit. Another issue that caused the breakup of a Siumut/Inuit coalition was the modernization of the radar facility on the United States military base in Thule. IA was opposed to the radar being part of the strategic missile defense system being developed by the United States. In the 2005 election, Inuit lost one seat to fall to seven of 31 seats.

#### *Demokratiit (Democrat) Party*

Per Berthelsen, who had been elected to parliament in 1999 as a member of the Siumut, left the party after two and a half years and ran as an independent in 2001 for the Danish parliament. The support that he has received has led to the formation of the Demokratiit party.

The first appearance in parliamentary elections for the Demokratiit was in 2002. The issues that year, according to media accounts, were independence for Greenland and the upgrading of the radar system at the military base in Thule. However, the Demokratiit campaigned on a platform that included addressing the housing shortage and infrastructure problems in Greenland as well as enhancing educational opportunities for native Inuits. Their platform attracted enough votes to earn them five of 31 seats. In 2005, media accounts of the election emphasized the diminishment of independence as a campaign issue and an increased focus on social issues. The Demokratiit earned enough votes to see their number of seats increase to seven of 31 seats. It received the second largest percentage of votes but is not part of the coalition government.

#### *Other Parties*

Greenland has had home-rule authority since 1979. Over that time, several political parties have emerged. While the Siumut, Atassut, Inuit Ataqatigiit, and Demokratiit parties are the dominant parties, there are other parties that have or are currently participating in Greenland politics. They include the Katusseqatigiit (Candidate Alliance), Akullitt Partiiat (Center Party), and Issittup Partiaa.

#### **United Mexican States**

Over the 196 years since independence from Spain was originally proclaimed on September 16, 1810, Mexico has seen many changes. Its borders have changed. The number of states has changed from 19 states, four regions, and one federal district to 31 states and one federal district. There have been at least four constitutions (1824, 1836, 1857, and 1917). The current one was adopted on February 5, 1917, and has been amended frequently.

The Mexican government is a federal republic with a bicameral legislature headed by a president who is elected to serve a six-year term. Prior to 2000, both parents of a presidential candidate had to be native-born Mexicans. Now only one does. The two chambers of the Union Congress (Congreso de la Union) are the Senate with 128 members and the Chamber of Deputies with 500 members. The members of the Senate serve six-year terms and members of the Chamber of Deputies serve three-year terms. Elections are held the same year as the president and at the middle of the president's term. Legislators cannot serve consecutive terms. Members of both chambers are elected through a combination of direct and proportional elections.

A series of dictators (often wearing the title of president) ruled Mexico from 1810 to 1929 when the National Revolutionary Party

(Partido Nacional Revolucionario-PNR) took control of the government. In 1946, it took its current name of Institutional Revolutionary Party (Partido Revolucionario Institucional-PRI). For the next half century the PRI would make Mexico one of the few dominant party democratic systems in the world. The PRI's structure and make-up exemplified the nature of the Mexican party system to come. Parties relied on strong individual leaders who could build broad coalitions rather than specify particular social groupings around which to articulate clear policy positions (Craig, 1992). Further, term limits were one of the rallying cries of revolutionary movements in Mexico. The result was some of the most stringent term-limit rules in the world. The term limits helped create a system in which politicians move horizontally (from one federal chamber to the other) and vertically (from one level of government [local, state, and federal] to another). The movement caused by this system helped to create a party machine with few rivals in democracies past or present. The PRI was successful because it was a coalition of government, industrial, labor, and agrarian leaders. Each had something to gain from maintaining or making only minor changes to the status quo. Internal party divisions, which often develop in dominant party systems, helped establish the roots for other parties later splitting off from the PRI to provide recent competitive party politics.

In the 1980s, 1990s, and 2000s, several factors contributed to the erosion of the power of PRI. The Zapatista National Liberation Army (Ejercito Zapatista de Liberacion Nacional-EZLN) led a still unsettled insurgency in the southern state of Chiapas. Many groups accused the PRI of rigging elections resulting in the creation of the Mexican Independent Federal Election Institute (IFE) in 1990. Various groups and political parties formed alliances with the intention of removing the PRI from power or

at least creating a viable alternative. In 2000, the erosion of power took its most visible step when Vicente Fox of the National Action Party (Partido Accion Nacional-PAN) was elected president of Mexico. PRI still controlled the Congress. In 2006, real ideological party competition surfaced supplanting multiple generations of one-party dominance.

#### *National Action Party (Partido Accion Nacional-PAN)*

As a reaction to the anticlericalism of the 1920s and the radicalism of the rule of General Lazaro Cardenas, the National Action Party (PAN) was formed in 1939. The entry of the PAN into Mexican politics marked the return of a conservative party. Its first victories came in 1946 when it won four seats in the Chamber of Deputies and two municipal governments. In 1988, PAN saw a significant increase in support rising from 10 percent of the seats in the Chamber to 20 percent. In 1999, PAN decided to form an alliance with the Democratic Revolutionary Party (Partido de la Revolucion Democratica-PRD) to present a single presidential candidate to face the PRI. Negotiations broke down and eventually PAN joined forces with the Green Party and other smaller parties to create the Alliance for Change. In 2000, Mexico elected PAN candidate Vicente Fox as president.

Initially PAN worked to restore many pre-Revolutionary powers to the church, especially regarding religious education and political participation. Their platforms were rooted in Catholic social principles within the principles of the institutionalized revolution. PAN is often described as a pro-business conservative party; however, they stress economic justice and equity. In 1969, at the 20<sup>th</sup> national convention of the PAN, they advocated that private property be viewed as

a good thing, but only if it contributes to the betterment of society (solidarismo).

In 2006, presidential candidate Felipe Calderon Hinojosa won a narrow victory. The presidential campaigns in 2006 had a decidedly negative tone. For example, Calderon was accused of giving contracts in the energy sector to his brother-in-law when Calderon was the energy secretary under Vicente Fox. Calderon denied any wrongdoing. Regarding foreign affairs, Calderon called for closer relationships with Mexico's Central American neighbors, Venezuela, and Canada. Specifically, Calderon wanted to create a second phase to the Plan Pueblo Panama which he claimed would unite Latin American countries in job creation, regional development, migration, and natural disasters. PAN also believed that the relationship between the United States and Canada should serve as a model for Mexico and the United States. PAN campaigned on keeping the Federal Electricity Commission (CFE) and national oil company (PEMEX) in state hands, but believed PEMEX should partner with private sector investors on refining, natural gas, and petrochemicals. The debate over partially privatizing PEMEX remains controversial.

#### *Party of the Democratic Revolution (Partido de la Revolucion Democratica-PRD)*

The Party of the Democratic Revolution (PRD) can trace its roots to a socialist conference in Mexico City in 1919 when the Communist Party of Mexico (Partido Comunista de Mexico-PCM) was formed. The standard bearers of the political left in Mexico took many forms over the ensuing years, but did not find much success until the PRD emerged in the late 1980s led by Cuauhtemoc Cardenas who had led a dissident group within the Institutional Revolutionary Party (PRI) called the Democratic Current (Corriente Democrática).

Cardenas was the son of former Mexican President Lazaro Cardenas. In 1989, PRD lost the race for governor in Michoacan to PRI. Fraudulent vote counting was widely believed to be the reason for the loss. In 1994, PRD won 71 seats in the Chamber of Deputies. That number grew to 125 seats in 1997. In 1999, PRD won its third governorship. In 2003, PRD representation in the Chamber fell to 95 seats.

PRD defines itself as a splinter group of the PRI, descendents of earlier socialist left political parties, and groups of socialist left workers, civic action groups, and peasants. While the earlier socialist left parties called for the state ownership of all businesses and services, the PRD is much more moderate. It has supported revolutionary movements such as the Zapatistas, but is more often typified by backing issues such as the reduction of the value added tax. It also has been generally supportive of the efforts of President Vicente Fox (PAN).

In 2006, presidential candidate Andres Manuel Lopez Obrador lost by less than one percent. AMLO, as he is often known, was a popular mayor of Mexico City and had been the early front runner for the 2006 election. The presidential campaigns in 2006 had a decidedly negative tone. Opponents tried to link AMLO to Venezuelan President Hugo Chavez and Zapatista leader Marcos and accused him of allowing crime to flourish during his time as mayor of Mexico City. AMLO denied any wrongdoing. PRD proposed studying mechanisms such as competitiveness funds used by the European Union to deepen the relationships between North American countries. AMLO viewed job growth at home as the best way to address the issue of Mexican migration to the United States. AMLO also pledged to provide poor people with tax breaks and to expand spending on social programs. The aim of

these actions was to lessen the gap between the rich and poor in Mexico.

#### *Institutional Revolutionary Party (Partido Revolucionario Institucional-PRI)*

In 1929, the National Revolutionary Party (Partido Nacional Revolucionario-PRN) was formed. In 1938, the party was redesigned and the name was changed to the Mexican Revolutionary Party (Partido de la Revolucion Mexicana-PRM). In 1946, it took its current name. The PRI began as a coalition of groups with their roots in the revolutionary period of Mexico's history. From 1929 to 2000, PRI was the dominate party in Mexican politics. It was not until 1988 that the PRI experienced a defeat at the state level. Shortly after that in 1997 it lost its majority in the Chamber of Deputies although it still retained a plurality. In 2000, PRI's demise continued when they lost the presidential election for the first time in 70 years. That same year the Alliance for Change gained a plurality of 223 seats in the Chamber and PRI saw its majority in the Senate disappear. In 2003, PRI saw a reversal of fortune when it came close to winning majorities in both chambers.

As the ruling party of Mexico for 70 years, credit (or blame) for most government programs should be given to them. PRI was responsible for the Mexican minimum wage, profit sharing for private sector workers, basic health care, and farms for peasants as well as encouraging foreign investment and privatizing many state interests. PRI has stressed Mexican independence from other countries, especially the United States, and promoted Latin American regional common markets while sympathizing with left-of-center Latin American governments.

In 2006, presidential candidate Roberto Madrazo came in a distant third place. For the majority of the campaign Madrazo was not considered a threat to win the election. His campaign attempted to cast PRI as the centrist

party capable of decreasing the polarization that was resulting from the campaigns of Felipe Calderon Hinojosa and Andres Manuel Lopez Obrador. The top foreign policy initiative for Madrazo was to rebuild a relationship with the United States by resolving border issues and developing a guest worker program. His economic policies would have focused on Mexico's global competitiveness. He included opening the energy sector of the Mexican economy to privatization as one way to improve things.

#### *Other Parties*

Although the PAN, PRD, and PRI are the dominant parties in Mexico, there are several other official parties currently active. They include Mexican Green Ecologist Party (Partido Verde Ecologista de Mexico-PVEM), Labor Party (Partido del Trabajo-PT), Convergence for Democracy (Convergencia por la Democracia-CD), Social Democratic and Farmer Alternative (Alternativa Socialdemócrata y Campesina), and New Alliance (Nueva Alianza). The last two were officially recognized in 2005. Several other parties have existed and several others still exist, but are not officially recognized.

#### **United States of America**

Thirteen colonies in North America declared independence from Great Britain on July 4, 1776. Those 13 colonies became the original states in the United States of America. From 1777 till 1789, the United States operated under a confederal system via the Articles of Confederation. On March 4, 1789, the current constitution went into effect. It has been amended 27 times, including the first ten amendments referred to as the Bill of Rights which were passed simultaneously with the ratification of the Constitution. The greatest growth in the number of states in the United States took place in the 1800s when the

country grew to 45 states. In 1959, the United States expanded to 50 states (the current number) with the admission of Hawaii.

The United States is a democratic federal republic with a president and bicameral legislature. The president is elected to serve a four-year term and is limited to two consecutive terms. The two chambers of the legislative body are the Senate and the House of Representatives. There are 100 members in the Senate. Two senators are elected from each state. They are elected to serve six-year terms. In even-numbered years one third of the seats in the Senate are up for election. There are 435 members of the House. The number of representatives from each state is determined by population. Representatives are elected from districts within each state. Districts have comparable populations. All members of the House are elected to serve two-year terms and are elected in the same years. Federal elections are held on the first Tuesday after the first Monday in November of even-numbered years.

In the United States, the diversity of immigration has meant that no single ethno-cultural cleavage has separated the country into firm party blocks. The social cleavages in the United States tend to be more fluid than the rigid divisions that developed into the party systems in Europe. Further, there has never been a socialist movement that took hold. Rather, the political culture of classic liberalism in the Lockean sense, has kept socialist or Marxist parties from taking root (Burnham 1974). This removes a key ideological source of party competition that developed in European socialist, social-democratic, and labor parties. Also, the right to vote has been broadly available, although it took some time for the franchise to reach some groups. Add to this the expanse of the country, regional distinctions, and availability of land ownership rather than feudalism, and American parties avoided many of the

ideological distinctions that exist elsewhere (Burnham 1974). Like Canada, the United States lacks strong working-class parties because of its "...early enfranchisement, high mobility, entrenched federalism, and marked regional, ethnic and religious diversity" (Lipset and Rokkan 1967:31).

Another impediment to party strength in the United States is the design of its political institutions. Key political leaders of America's founding distrusted political parties and built institutions that would undermine them. James Madison, a key architect of the American Constitution, openly promoted the new political system as a way to undermine what he called factions, and what we might call parties or interest groups today. America's first president, George Washington, devoted his farewell address to two major themes: avoiding international entanglements and avoiding the development of political parties. This distrust of parties is woven into American political culture and its federal institutions. Additionally, American parties were formed and reformed to meet particular goals of politicians rather than as mass political movements. As a consequence, they have realigned numerous times by fundamentally shifting the social bases of party support and party goals. Finally, the progressive reforms that instituted democratic selection of political party candidates rather than party-elites choosing candidates has meant that maverick candidates who do not stick to a party's ideological approach may and do win election without punishment from the party. Elsewhere, parties choose (and remove) their candidates or need only produce a party list that voters vote for rather than candidates, which insures that the party can purge any non-ideological adherents (Dalton 2002:126-127).

Although there are more than two parties in the United States, it is for all intents and



purposes a two-party system. For example, the federal and state rules and regulations governing elections put oversight authority in the hands of representatives of the Republicans and Democrats. As further evidence, consider that no other party has controlled either chamber of the federal legislature or the presidency since 1855. Direct elections and single-member districts contribute to the perpetuation of the two-party system.

In spite of the fact that many elements of the system are set up to benefit the two main political parties, there is not nearly as much party discipline as can be found in other countries. Part of the reason for this is that the national parties are a coalition of state parties which are a coalition of local parties. The ideological differences that can be found between regions, the fact that much of the available patronage comes on the state and local level, and that the state and local parties can drive who is nominated to the Senate and House weaken party discipline.

Taken together, these factors have meant that American political parties are not very programmatic compared to other party systems. Indeed, an influential group of American political scientists wrote a seminal piece arguing for reforms toward more programmatic U.S. parties entitled: "Toward a More Responsible Two-Party System" (Committee on Political Parties 1950). But it would be incorrect to say that parties have no effect on policy. On average, when the president and Congress have been of the same party over the past fifty years, the president has had much greater success passing his agenda. Further, in recent decades these parties have become more ideologically unified as southern conservative Democrats have left the party or become Republicans. This has resulted in greater partisan divisions and competition in presidential elections and the ideological divisions in congressional

voting have never been greater in the modern era (Davidson and Oleszek, 2006:284-5).

The Republicans controlled both chambers of the legislature and the presidency from 2003 through 2006 when the Democrats took control of both chambers. Neither party controlled all three from 1981 to 2003. The Republican Party controlled the House from 1995 to 2007. The Democrats controlled it from 1955 until the 1994 election. Since 1981, control of the Senate has changed hands six times. The Democrats controlled it from 1955 until the 1980 election. Since that pivotal election of 1954, there have been six Republican presidents and four Democratic presidents.

In 2008, a member of the Senate almost assuredly will be elected president. This will be the first time since Richard Nixon (1969-1974) that a current or former member of the Senate will be elected president.

### *Republican Party*

The Republican Party traces its roots to the Federalist Party led by Alexander Hamilton. The present-day Republican Party was formed in the 1850s as an anti-slavery and pro-protective tariff party. It could be argued that the Republican Party was a third party that found significant electoral success, but it would be more accurate to argue that it emerged as the result of a split in the Whig Party and major issues of the day. By 1855, it replaced the Whigs as one of the two major political parties and became the majority in the House that same year. In recent years, it often has found its greatest support in rural areas, suburbs, and small towns.

Today, typically viewed as the conservative party in the United States, the Republican Party has tended to support pro-business legislation, welfare reform, and changes to the tax system, including reductions or the elimination of the estate tax and capital gains tax. While most

Republicans agree on less government control of the economy, they often are divided on government control of individual lives and the social order. Traditional Republicans tend to support less government control in these areas, but a group of Republicans that has been labeled the Religious Right favors much more government involvement in social and moral issues.

In 2000, President George W. Bush was elected in a controversial election. He received 47.9 percent of the popular vote (less than Democrat incumbent Vice President Albert Gore), but 271 electoral votes which was sufficient to win the election. In 2004, President Bush was reelected with 51 percent of the popular vote and 286 electoral votes. That year the Republican platform included stimulating economic growth by constraining discretionary government spending, making certain temporary tax cuts permanent, and extending and expanding certain advantages to small businesses. Their foreign policy positions centered around what the Republican Party called the “war on terror.” They supported action against foreign states that supported terrorism and pledged to support the rise of democracy throughout the world. They continued to stand behind the No Child Left Behind Act of 2001 as the way to improve the United States’ education system. They also campaigned that they would amend the Constitution to state that the Fourteenth Amendment applied to unborn children.

In 2008, Arizona Senator John McCain received the Republican nomination for president. Three prominent issues were the economy, health-care, and national security. Senator McCain proposed a summer gas tax holiday and a plan for trading non-conventional mortgages taken after 2005 for new 30-year mortgages with more favorable terms as ways to address immediate concerns. His long-term strategies included lowering trade barriers, repealing the alternative

minimum tax, and tax credits for research and development efforts. His health-care initiatives included a tax credit to offset the cost of health insurance, an expansion of health savings accounts, and lowering costs through improved competition. His national security plans included the development of a missile defense system, increasing the size of the military, and modernizing the military to meet the most likely forms of conflict today.

### *Democratic Party*

The Democratic Party traces its roots back to Thomas Jefferson and Andrew Jackson. It started out as a congressional caucus opposed to Alexander Hamilton’s economic policies and broke from the Democratic-Republican Party after the contentious election of 1824. The party name, as it is seen today, can be found as early as 1828 with the election of President Andrew Jackson. It often has found its greatest support in large urban areas of the Northeast and West Coast.

Today, typically viewed as the liberal party in the United States, the Democratic Party has tended to support a progressive tax structure, established the Social Security system, and supported the creation of various social welfare programs such as food stamps and Head Start. While most Democrats agree on more government involvement in control of the economy, they often are divided on government control of individual lives and the social order. A moderate group of the Democratic Party known as the Democratic Leadership Conference, tends to support some government involvement in these areas, but the liberal wing favors very little government involvement in social and moral issues.

In 2004, Senator John Kerry became the second Democrat in a row to lose a presidential election to President George W. Bush. That year the Democratic platform called for a tax increase for people making

over \$200,000 annually. Additionally, they wanted to change tax policies that encouraged companies to close US operations and export the jobs to other countries. The Democratic platform emphasized diplomacy, tolerance, and understanding when discussing foreign affairs. It also focused on energy independence as a key to both economic growth and foreign affairs. The Democratic Party did not oppose the No Child Left Behind Act, but they did claim that President Bush had not fully funded the effort. They pledged to find the funds. Their platform included a statement that “abortion should be safe, legal, and rare.” They supported a woman’s right to make decisions regarding abortion and supported family planning and adoption incentives.

In 2008, Illinois Senator Barack Obama won the Presidential election for the Democratic Party. Ethics reform, health-care, the economy, and international relations were among his top issues. During the campaign, Senator Obama stated that he would not accept campaign contributions from political action committees or lobbyists. He proposed centralizing ethics, lobbying, and campaign finance information in a searchable database. He supported publicly financed campaigns and free television and radio time for candidates. His health-care plan included universal coverage funded in part by fees paid by employers that do not offer health insurance. His economic initiatives included using foreign trade to promote labor and environmental standards around the world, pressuring the World Trade Organization to enforce trade agreements, and providing incentives to boost renewable energy consumption to 25 percent of all energy consumed by 2025.

#### *Other Parties*

The Republicans and Democrats are the dominant political parties of the United

States, but there are other active parties. These include the Constitution Party, Green Party (partner of the European Federation of Green Parties and the Federation of Green Parties of the Americas), Independence Party, Libertarian Party (viewed as the largest third party in the United States), National Law Party, Reform Party, and Socialist Party.

#### **Conclusion**

Differences in society, economy and polity among North American democracies lead to elements of distinctiveness from other areas of the world. Rather than party systems being built from established social cleavages, party competition has been more fluid and often reflects greater regionalism and pragmatism relative to other areas of the world. Interestingly, the fragmentation of the party systems of other advanced industrial democracies has often produced the same type of catch-all party that has existed in North American countries, especially in the U.S. and Canada. Ironically, this has happened as parties have become more programmatically disciplined in the U.S.

Regardless of the similarities and differences between these countries there is one overarching theme that can be found in each in the early 21st Century. All four countries have seen more competitive elections and shifts in party control. Canada and the United States saw control shift from the main liberal parties to the main conservative parties. Mexico saw the Institutional Revolutionary Party (PRI) lose the presidency and control of the Chamber of Deputies after 70 years of dominance. In Greenland, the Siumut Party continued to hold the largest percentage of seats in the parliament, but the seats are almost equally balanced among four political parties. With the shifts in control have come shifts in policy directions. The success or failure of those policies will determine how long the parties

are able to stay in power, but it is unlikely to return to the long periods of party dominance that were seen in the 20th Century.

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## North-East Asian Democracies: Politics and Policies

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Exploring a concept on a regional basis inevitably raises the issue of how one discusses its significance in a way that doesn't simply reify the mere coincidence of geographical proximity (Buzan 1998:68). This issue confronts one with the question, *what makes a region a region*, what do its nation-states share that makes it reasonable and explicable to group them in some ways and differentiate them in others? This question of classifying aspects of a 'region' has been particularly relevant to our understanding of East Asian governance. Here, the idea of the 'strong state' has been used to identify some shared elements between the otherwise quite different political systems in Japan, South Korea, and Taiwan. According to Case, state strength can be defined as "the capacity of state actors and state institutions to *autonomously* devise and implement public policy; shaping the preferences and interests of other actors; intervening in and transforming economic and cultural structures." (Case 1998:251). The two key components of the strong state concept are:

1. A relative *coherence* in policy, entailing some combination of a long-term strategy and continuity of personnel and political parties in power.
2. A degree of *insularity* in policy from both domestic and international pressures to change tack.

For much of the last 50 years these two components of the strong state concept have seemed particularly relevant to the authoritarian and paternalistic political systems and political cultures of East Asia. In conjunction with ideas of market "market conforming" strategies, the dynamism of the

developmental models of the region, "the East Asian economic miracle", as it was, has often been attributed to the strong state concept. The concept of the strong state seemed to seamlessly segue into that of Confucian capitalism (Whitley 1998; Tu 1989), despite the fact that precisely the same characteristics had been criticised earlier as impediments to development (Dirlik 1995). Of more immediate analytical importance however, is that as we progress into the twenty-first century the strong-state concept seems to capture less and less of the realities of East-Asian state governance.

East-Asian politics in the democracies of Japan, South Korea, and Taiwan seem to be in the early stages of significant changes, addressed sequentially in § 1-3. Since World War II, Japan has had a political system and political culture conducive to soft authoritarianism in the guise of conservative paternalism. This has allowed a high degree of policy continuity. However, Japan's mounting economic problems throughout the 1990s have forced the issue of basic changes in governance to the fore. South Korea, by contrast, was a more hardline authoritarian dictatorship until the democracy movement of the 1980s and the democratisation of the presidential system in the 1990s. However, democratisation in South Korea faces similar economic challenges to Japan, and shares some common aspects of political culture and governance. More importantly, addressing its problems has similarly raised the issue of how vested interests and sources of previous success that now seem to be impediments can be overcome. Here South Korea shares with Japan an opening out of the political landscape and what seems to be a trend towards greater democratic accountability embodied in new kinds of politicians and popular political attitudes. In some respects Taiwan provides a different case. Most notably, the basis of its economic

development has been quite different and thus has not energised political discourse to the same degree on the basis of basic structural economic issues. However, the legacy of one-party authoritarianism, including the role of business in politics, and its divided nation status does provide for certain similarities with South Korea in the subsequent development of a democratic political system.

## 1. Japan

The Japanese political system is one of representative democracy. Its constitution, written in 1947 during the American occupation (1945-1952) under General MacArthur, defines the basis of the system (Eccleston, 1995). It features a bicameral legislature, called the *Diet*. The lower house, or House of Representatives, is the more powerful house. It contains 480 seats, with 300 of the elected MPs in single-seat constituencies, and the remaining 180 chosen by proportional representation amongst the political parties. The upper house, or House of Councillors, serves an equivalent check and balance function to the British House of Lords or the American Senate. Since 1983 it has been elected entirely by proportional representation. One half of the House (121 seats) is elected every three years. Suffrage begins at 20 years of age, the legislature appoints the prime minister, reflecting the distribution of seats in the two houses, and the prime minister appoints the executive. Each cabinet minister is the head of a ministry responsible for some aspect of the state.

Clearly, the formal architecture of the Japanese political system follows a broadly Western model. However, the system and the political culture have exhibited a number of features conducive to categorising Japanese governance in terms of the strong state concept. Japanese politics have been dominated by the Liberal Democratic Party

(LDP) since its formation in 1955. The LDP held unbroken power for 38 years from 1955 to 1993. The LDP returned to power in 1996 and has subsequently governed through a series of coalitions, principally with the New Conservatives and the Clean or Komeito Party. Japanese politics is also highly dynastic and nepotistic. Three out of the past four prime ministers inherited their party constituency seat from a relative. The current prime minister, Koizumi Junichiro, is a third generation MP. Of 323 LDP candidates at the last House of Representatives election in 2003, 116 were second or third generation candidates (Parry 2003a). There is, therefore, a high degree of continuity in Japanese politics. This situation has been facilitated by a combination of the formal electoral rules and the political culture. Japanese electoral rules have, boosted by the 1994 electoral reforms, only allowed formal campaigning for one month before the election and have placed limits on campaign expenditure, the number of speeches that can be made and the amount of advertising that can be undertaken. The low key nature of campaigning has, therefore, tended to favour incumbents. This tendency is further reinforced by a political culture rooted in tradition, trust and respect. Individual candidates tend to campaign on local issues and exploit local networks of longstanding relationships in civil society. This strategy tends to reflect the way voters place a great deal of emphasis on the grassroots status and track record of candidates and their families.

The net result of these characteristics has been a political culture of soft authoritarianism in the guise of conservative paternalism. This has been conducive to a high degree of policy continuity. However, there has been a certain degree of tension surrounding the emergence of this continuity. Japan has had eleven Prime Ministers in the last fourteen years. Moreover, since

parliamentary candidates tend to campaign on a local basis there tends also to be a significant diversity in the way MPs of the same party vote on issues in the two houses. Accordingly, with the exception of the vocal minority Communist Party (which usually has around 10% of the vote), the parties are best seen as looser groupings than the more strongly aligned western political parties with their more clearly delineated ideologies and disciplinary systems that direct their MPs voting behaviour. Over the last 50 years this tension has been resolved at the executive level. The high degree of continuity in government (if not always and recently personnel) has allowed for long-term development strategies. Moreover, although the *Diet* enacts law, the legislation is drafted by career officials in each ministry where continuity is provided by powerful civil servants in vice-minister positions and as director-generals of bureaus within each ministry.

The Ministry of International Trade and Industry (MITI) and the Ministry of Finance (the *Okurasho*) provide archetypes of how this power is diffused through a broad system of governance in which politics and economics are merged. MITI, established in 1946, has been the key administrative institution for industrial policy (*sangyo seisku*). MITI has wielded a number of policy instruments, such as joint ventures with the state, patent rights, and conditional technology transfer. More importantly, however, it has straddled the public-private divide through a network of relationships, founded in consultative-advisory committees, with the large *keiretsu* Japanese industrial combines. Through this combination of formal and informal avenues it has helped to mediate a consensus-based economic policy strongly focussed on long-term low interest rate investment in rapid productivity growth in export oriented markets (Johnson

1982,1995). The Ministry of Finance has complemented this strategy (though not without a degree of bureaucratic competition between the two ministries). The *Okurasho* provides a similar function for the commercial banks and life insurance firms, as well as intervening in the Japanese stock market and the exchange rate in accordance with fiscal and monetary policy (Hartcher 1997). As a subsidiary function the Ministry has also pursued a strategy of seeking to appoint its former employees to key posts in other ministries, public corporations and private firms—a practice known as *amakudari*, or the descent from heaven. Masaru Mizuno, for example, from the Ministry's tax bureau, was appointed president of the state-owned Japan Tobacco in 1994. MITI and the *Okurasho* illustrate, therefore, how policy coherence has been sustained in a political economy. This might be conceptualised as a combination of Weberian and Foucauldian power. Weber provides the concept of bureaucratic power as a top down, clearly defined hierarchy of rigidly enforced and clearly defined rule systems (Weber 1946:232-235). Foucault, provides the more amorphous concepts of power/knowledge and the flow of power into the capillaries of society where it is internalised providing a self-disciplining subject (Foucault 1980:59-60). In both cases there is a clear resistance to change.

Change, however, has increasingly become an issue. Though the successes of the Japanese developmental model in the 1970s and 1980s are well-documented, it remains the case that sources of success can become the origins of failure when other conditions change. The long-term nature of Japan's economic strategy facilitated by political continuity and close public-private ties, have generated a powerful coalition of intransigent interests in the face of economic problems. This first started to come to the fore in the



late 1980s. In the wake of the appreciation of the yen following the 1986 Plaza Accord Japanese industry increasingly followed a strategy of foreign direct investment, diversifying production abroad—in order to avoid the downturn in the terms of trade that appreciation created and also to exploit low wages in East Asia and side-step protectionism in Europe and America. This set the scene for the possibility of unemployment. By 1990, moreover, economic growth was slowing, and the Japanese economy was hit by a number of financial scandals, insider share dealing, bureaucratic corruption, and a damaging property speculation that set off a liquidity crisis requiring the state to push \$18 billion of taxpayers' money into the financial system. This set a precedent for the Ministry of Finance to continue to transfer state pension assets to bail out the system throughout the 1990s. At the same time, the *keiretsu* and state-owned companies failed to react to slow economic growth by rationalising loss-making subsidiaries. The 1997 East Asian financial crisis simply exacerbated this situation. The Japanese stock market crashed. Since the Japanese banking system is based on capital asset valuations linked to the stock market this further reduced the capacity of the system to cover losses. However, the *keiretsu* continued to pursue a strategy whereby the larger corporations cross-subsidised and/or disguised losses whilst the state guaranteed loans to small and medium firms (tied into the *keiretsu* supply chain) who seemed crippled by chronic shortfalls in demand. These strategies used the same links that had previously allowed for successful cooperation and financialisation. Japanese political and economic governance was seemingly insulated from policy pressure for change precisely because of its previous success and the nature of the political system and political culture.

This situation has produced a new context for the political parties of Japan and a new set of challenges. Though there is still a strong generational and hereditary nature to politics in Japan, there has been a significant erosion of trust in figures of authority. The percentage of eligible citizens participating in voting at elections has fallen through the 1990s to a low of 60%. The decline in trust reflects a catalogue of failure to come to terms with bureaucratic insularity exposed by economic crisis. This was first highlighted in 1993 when the LDP was ousted from office for the first time since 1955. Morihiro Hosokawa, after 20 years in various aspects of government as a member of the LDP, split to form his own Japan New Party in 1992, and led a coalition to election victory the following year, becoming Prime Minister on a “not the LDP” ticket. His anti-corruption agenda and commitment to break the power of the ministry bureaucracies (especially the Ministry of Finance) found favour with both domestic voters and the Clinton administration (who referred to the ministry as Japan's “permanent government”). Hosokawa was forced to resign in 1994 facing his own corruption charges. However, bureaucratic insularity had at least become both a subject of media scrutiny and a political issue that the parties could not thereafter ignore. Accordingly, one might argue that the system is in the early stages of opening out and that Japan has begun to deviate from the domestic insularity characteristic of the strong state model.

One sees this opening out for example in 2001. In that year the LDP forced the resignation of Prime Minister Mori Yoshiro and in an unusual move, his successor as LDP leader and thus PM, Koizumi Junichiro, was selected in an open process of election amongst LDP members and then LDP MPs (Lincoln 2002). Koizumi is an altogether new kind of politician for Japan. He blends



traditionalist credentials as a third generation politician, with 30 years in the *Diet*, with a Western style campaigning strategy, a media-friendly face that can be seen everywhere from on biscuit tins to key rings, and a reputation for cautious radicalism. In the neoliberal vein he has advocated privatisation of certain public corporations, for example, but has stuck with a Keynesian fiscal policy of public works. Though taking the radical step of appointing women and academics from outside the political establishment to key posts he has also been careful in his choice of ministers to maintain a balance between the different factions of the LDP and other parties. He is also pragmatic enough to court conservative opinion by visiting the controversial Yasukuni war shrine and accepting retrenchment – firing his publicly popular female Foreign Minister Tanaka Makiko in 2002 when her criticism of the Ministry of Finance threatened to damage his attempts at incremental reform (Uriu 2003).

The crucial questions for Japan are whether the political parties have any genuine sense of what is needed to rectify their economic problems and indeed whether there are any domestically based solutions at all. Koizumi and the LDP seem committed to a kind of experimental incrementalism—a little privatisation here, some fiscal stimulus there, a slow turnover in bureaucratic personnel and practices, and greater accountability in government. However, for the first time in the modern period, Japan now has a credible opposition (rather than coalition of competing minority parties) in the form of the Democratic Party of Japan (DPJ), gaining 40% of the seats in the Lower House elections of 2003 (Parry 2003b). It also has, for the first time in over a decade, a credible and charismatic opposition leader in Naoto Kan, able to rival the new style of Koizumi. Koizumi now faces the problem that domestic pressure for reform may force rapid policy

changeover in quite a different way than was the case in the past. A more accountable system may therefore come with costs if the LDP and DPJ begin to trade power and lack effective policy strategies. This may be a new downside, an unanticipated consequence of the move away from a form of strong state. Whether this is so remains to be seen, but the problems to be overcome are vast and intimately tied into the world economic situation in a way that may offset domestic solutions:

- Japan was in recession at the beginning of the 21<sup>st</sup> century. Economic growth 2000-2002 has run at -1 to -2%, though there has been some slight recovery 2003-2004. Since Japan traditionally has a high marginal propensity to save and relatively low consumption it has not been easy to stabilise the economy through boosts to private spending. This is quite unlike the growth of debt-credit consumption patterns of the UK and USA which have sustained their economies through recent periods of low business investment. Moreover, much of Japanese manufacturing is export oriented. Therefore, the fall in world demand, particularly in the car and hi-tech markets has exacerbated the problem of low demand. From 1998-2003 industrial production fell by 9.3% (Richter 2003). This falling growth means falling corporate revenues and falling tax revenues reducing the capacity of the state to spend without generating debt.

- Unemployment in Japan now exceeds 5% - a record post-war high for a traditionally full-employment economy. In a certain sense this is slightly offset by a falling birth rate and an aging population. However, this in itself produces a long term demographic and fiscal problem that a smaller working population (with higher unemployment) must pay the current pension provision of an expanding retired population.

- To forestall rapid growth in unemployment the state has not pursued rapid and widespread neoliberal style rationalisations and privatisations. Rather it has followed an expansionary Keynesian public works strategy based on not necessarily “needed” large-scale road and construction projects. During the 1990s successive governments have spent over \$1 trillion dollars on public works and a million jobs have shifted from the private sector to construction, undertaken by the public corporations (Righter, 2003). Since tax revenues are falling the government is running large fiscal deficits to finance expenditures that have yet to show obvious multiplier effects and that may not see the deficit recouped through subsequent tax revenues. The debt problem may therefore be structural and cumulative rather than cyclical and balancing over time. In 2001 Japan ran a 7% fiscal deficit, cumulative debt stood at 135% of GDP, rising to 140% in 2003.

- Also to forestall rapid growth of unemployment the state has allowed large public and private corporations to accumulate debt. The state has provided over \$40 billion directly in temporary loan guarantees to firms and has allowed a regime of soft debt by the 115 regional banks. Government estimates of non-performing loans (NPL) are continually being upgraded but constantly lag behind private estimates. In 2001 the state Financial Services Agency placed NPL at 20 trillion Yen (\$150 billion). Private estimates range to \$1 trillion.

- Awareness of the existence of these NPL and the poor growth performance of the Japanese economy has tended to reduce the value of the Japanese stock market. The Nikkei fell to around 20% of its 1989 high in 2002. The collapse of the Nikkei reduces the capitalisation of the banks. This increases the problem of NPL. This in turn has forced the state to underwrite the private banks. Until

recently the banks included NPL as “deferred tax assets” in their accounts allowing them to enhance their apparent capitalisation. In December 2003, auditors of Ashikaga Bank, the tenth largest bank refused to allow this practice. The bank was revealed as insolvent and was summarily nationalised. The bailout cost the state \$5.3 billion and reflects a basic structural problem with the whole finance industry (Lewis 2003). The very need to intervene further affects confidence in the stock market.

- The collapse of the Nikkei has also been associated with general deflation or falling prices. Falling prices reduce corporate revenues and tax revenues and, since each yen is now worth less, increase the real cost of accumulated debt.

- To try to forestall deflation, create some small inflation, to try to stabilise the Nikkei and to reduce the increase in NPL, the Bank of Japan has felt it necessary to pursue an expansionary monetary policy based on zero to negative interest rates. The Ministry of Finance continues to pump public money into the Nikkei and the public corporations to prevent firms becoming insolvent in a way that would spark off a stock market, banking, and *Keiretsu* collapse. So far the banks have written off £575 billion of bad-debt, subsidised by £200 billion of public money (Righter, 2003). The Ministry of Finance has also tried to improve the export prospects of Japanese firms by using its currency reserves to buy the \$ and thus raise its price against the yen. This increases the ability of American consumers and those whose currencies are pegged to the \$ to import the now relatively cheaper Japanese products. However, the \$ has tended to fall in value since the September 11<sup>th</sup> terrorism attack making this an expensive policy. The Bank of Japan spent \$150 billion in 2003 to prop up the \$. If the \$ falls despite the intervention then effectively Japan is losing money by buying \$s. Total

losses in currency interventions at the end of 2003 stood at \$50 billion. The Bank has vowed to end this policy, partly because it provides speculators with a degree of certainty that any volatility they create will result in the Yen re-appreciating allowing them to profitably second guess the market at the tax payer's expense. The Bank has yet to be tested on its pledge.

What this locus of problems suggests is that the task of keeping the Japanese economy afloat in the short term has required that the LDP and its coalition partners *not* act to rapidly reform the system of economic and political governance. The current economic orthodox medicine of neoliberalism would surely make matters worse since a reduction in budget deficits and the withdrawal of capitalisation from the banks and corporations would spark mass bankruptcies and unemployment. In a sense the parties have waited too long to tackle the problems in terms of the kind of widespread rationalisation and privatisation policies usually urged by the IMF, the US Treasury and influential academic economists. Given the failure of these policies elsewhere this may be a blessing in disguise. It may also mean that Japan still requires a degree of insularity in its receptiveness to international pressures for policy change in the economic sphere. It may therefore be that effective political and economic reform (whatever that might be) can only come in Japan hand-in-hand with renewed economic growth from a recovery in world demand. This is quite different, however, than Japan's relationship with the USA on security issues. Here, for example, Japan has succumbed to growing pressure since the end of the Cold War to undertake constitutional change to allow the build up of Japanese armed forces. Such forces would shoulder some of the burden and cost of maintaining the security of East Asia and would undertake overseas 'police

actions' either as part of UN missions or as part of a US coalition (Buzan, 2003; Uriu, 2003). Here, ironically, Japan may become militarily strong precisely by diverging from its strong state status.

## 2. South Korea

In economic terms, the Republic of Korea or South Korea faces very similar challenges situated to similar economic and bureaucratic economic-political structures as Japan. Its *chaebol* are analogous to the Japanese *keiretsu* and stand in a similar relationship to an unravelling of the strong state in a developmental model built on export-orientation (Kim, 1991). The *chaebol* received key impetus from policy directed loans from state-owned banks based initially in heavy manufacturing, cars and shipbuilding but shifting in the 1980s into hi-tech markets such as computer chips. As with Japan, the nature of the public-private relationship, particularly of the larger *chaebol* (Hyundai, Samsung, LG and Daewoo) has come under increasing scrutiny in terms of public-private contracting, the provision of loans, and more primitive accusations of bribery and profiteering (Clifford, 1994). As with Japan, questions of basic structural changes to the economy and a growing public intolerance of practices that are increasingly seen as self-serving or corrupt have become central to political discourse.

The South Korean political system, that is attempting to make sense of these problems however, is somewhat different in origin than that of Japan. It was as a result of the end of Japanese occupation that South Korea became a Republic in 1948. The Korean War (1950-1953) belatedly (after its initial neglect by Truman) brought South Korea within the security perimeter of the US, under the aegis of the UN, during the Cold War. Whilst there is some similarity to Japan here in the sense of a security relationship to the US, South

Korea was not subject to a non-militarised constitution nor did something as explicit as the Yoshida Doctrine define its development. Instead, the 1953 Panmunjom truce left Korea divided at the 38<sup>th</sup> parallel with no machinery in place either for constructive dialogue or conflict resolution between the two Koreas until 1997. The South Korea that emerged from the war was considerably less stable than Japan and the US did not apply the same kind of leverage to create a form of viable representative democracy. Instead, South Korea emerged as a far more hardline authoritarian state. Accusations of election rigging and corruption dogged the presidency of Syngman Rhee (1948-60) and in 1961 a coup resulted in a military dictatorship in all but name under President/General Park Chung Hee until his assassination in 1979 and, after a further coup, Chun Doo Hwan until 1987.

Thus, though economic success was in many respects similar (by the time of the East Asian Financial Crisis of 1997 South Korea had risen to be the eleventh largest economy in the world) strong state policy coherence and the insularity of policy in South Korea derived from quite different sources than in Japan. Furthermore, civil unrest has played a greater role in political change. Though Hwan's successor in the election of 1988, President Roh Tae Woo was hand-picked and backed by the military, commentators suggest that it was the growth of civil society as a byproduct of development, including the growth of an educated middle class and a propensity for widespread student demonstrations that forced the beginnings of democratisation of the presidential system (Case, 1998; Kim 2000). At the same time, it was dissatisfaction with the lack of a free press, the poor level of social security, the lack of independent trade unions, low wages and an average 72 hour working week, in an increasingly wealthy nation that spurred that

militancy—a militancy that the military were reluctant to continue to suppress since they feared damaged relations with Western trading partners. The decline and then collapse of the Soviet Union in 1991 and the end of the Cold War also reduced the state's leverage in resisting calls for democratization, in terms of the dictatorship's security value to the US.

In 1993 Kim Young Sam was elected as the first civilian head of state in South Korea for 30 years. The system that has subsequently developed has, like Japan, had to confront the problem of how to reconcile the perceived need for basic economic changes, particularly in the wake of the East Asian Financial Crisis of 1997, with greater political accountability (Oh, 1999). Unlike the Japanese system, the South Korean legislature is unicameral. The national Assembly consists of 273 members serving a four year term, 84% of seats are by direct election on the basis of electoral districts with the final sixth distributed proportionately to the vote amongst parties winning 5 or more seats. 16 standing committees, mirroring the different bureaucratic ministries, serve the function of an upper house in scrutinising bills. The executive is headed by the president, elected separately, who is nominally a non-partisan presence amongst the political parties. Typically, the president is a senior member of one of the political parties who though endorsed by given parties takes up a “neutral” stance at the time of Assembly elections. The president has supreme power to formulate and propose policy, and appoints a prime minister (effectively his aid) and two vice prime ministers, in conjunction with whom he appoints a cabinet or State Council of 15-30 ministers who head the different functional ministries.

Structurally, there is clearly a greater potential for more centralised government

here than in the Japanese system. In some respects, however, this disguises some basic affinities with Japanese governance and Japanese political culture. As in Japan, policy continuity has been maintained by a tenured and powerful civil service. The civil service is informally and formally linked to business through the state banks and the *chaebol* via a cross-mapping of personnel exchanges, common schooling, and a series of longstanding consultative committees and relationships. As in Japan, the grouping of political parties has been narrow and ideologically vague.

In South Korea, however, this lack of clear defining ideals is also linked to instability characterised by short-lived political parties. Despite the vibrancy of grass roots civil society organisations, which one might think indicates well-formed and differentiated political philosophies, political parties lack cohesion. Though membership is large, running into the hundreds of thousands, ordinary members tend not to pay dues, select candidates or, in keeping with ideological ambiguity, directly determine a policy platform. People have tended to join parties on the basis of personal connections, particularly regional and corporate affiliations, and because of a particular charismatic leader around whom the party is constructed, often with the backing of a *chaebol*. Shifting coalitions and factions and an absence of core political values mean that parties are constantly merging and being reformed.

Yet, with the concept of continuity in mind, to some degree the instability of parties has been superficial in terms of the range of policy since the same candidates from the same families continue to emerge, backed by the same conglomerates, meaning that however voting patterns fluctuate a relatively conservative National Assembly has resulted. As in Japan, this has become more of an

impediment with the emergence of fairly fundamental economic problems in the 1990s. The net effect has combined the Japanese problem of the difficulty of addressing entrenched public-private vested interests from within the system, with a particularly vicious form of factional politics focussed on the personal activities of party leaders their client-patron links and their families. This has created a voting climate of cynicism where the electorate openly question what their National Assembly is for (Ha, 2002, p. 62) - though turnout is still over 70%. Policy change is additionally hampered by the possibility, as in the US, of the president confronting a hostile National Assembly since elections for the two are staggered and factions, coalitions and voting patterns can switch quite quickly.

Whereas in Japan a decline in political trust has been a consequence of the failure to come to terms with problems of bureaucratic insularity, exposed by economic crisis, in South Korea, that lack of trust has emerged with the democratic system itself and derives both from the legacy of a militarised authoritarian strong state and the characteristics of the democratic political structures and culture that have replaced it. However, one can still argue that South Korea, like Japan, has begun to deviate from the domestic insularity characteristic of the strong state model.

At the time of the December 2002 presidential election, amongst the 8 or so contemporary political parties, the two major parties were the New Millennium Democratic Party (*Sae Cheonyeon Minjudang*; NMDP) of then President Kim Dae Jung (1998-2002), the long-time adversary of the dictator Park Chung Hee, and the Grand National Party (*Hannara Dang*, GNP) structured around the legacy of Park and with close links to the military. Coming immediately on top of the East Asian Financial Crisis, the four year Kim

administration had had a difficult time. Despite a few policy endeavours and some economic recovery it was perceived to have failed to effectively deal with basic structural problems with *chaebol* debt, bank liquidity and public-private graft (Ha, 2002). It had also been dogged by scandal as many close to Kim, particularly through his Peace Foundation were investigated for selling presidential influence—most notably his second son, Kim Hong Yup, who received a four year prison sentence (Lee, 2003).

In elections of August 2002 the GNP wrested control of the National Assembly from the NMDP producing a hostile parliament. With Kim stepping down as president, the NMDP took the unprecedented step of fielding several candidates in primaries who would be openly elected by ordinary citizens for the party's presidential nomination. Just as with the election of Koizumi this threw up some atypical candidates, including Roh Moo-Hyun, a 56 year old human rights lawyer and labour activist. Roh gained the nomination on a wave of support from the "386 generation" of disenchanted thirty-somethings who had participated in the democracy movement of the 1980s. The sense of expectation around Roh allowed effective mobilisation of civil society organisations around him through the Internet, bypassing the official media. A *Roh sa mo* (gathering of those people loving Roh) web site and chat room campaigned on his behalf and despite losing some credibility through Kim's patronage (his son's corruption scandal was contemporaneous) Roh beat off a late challenge for the presidential nomination from a son of the founder of Hyundai and went on to a narrow 2.3% victory over the GNP chairman Lee Hoi-chang in December.

The election was in some ways a demand for change and greater accountability by the electorate. Roh was an obvious non-

conformist choice, irrespective of whether he was NMDP or GNP, whilst Lee, a former Supreme Court Justice, represented the status quo. On this basis voting tended to be generational, but it also reflected a degree of continuity in terms of a broad regional split based on the power bases of the parties and Roh also benefited from some typically scurrilous NMDP orchestrated attacks on Lee's integrity in the media—in a timely intervention his sons were accused of dodging military service.

The perceived need within the NMDP to open up the nomination process and Roh's subsequent election, one might argue embodies a possible opening out of Korean politics. In some respects Roh's election seems a seminal event. However, it might also be understood as a small yet significant incremental shift indicating greater pressure on the political establishment to make good on initiatives aimed at acknowledged problems.

A key problem, as in Japan, has been the implementation of reform of the conglomerates, such as the 2001 proposals to impose a maximum debt-capital ratio (200%) and ceiling limits on investments. Such dry seeming issues are of central electoral importance when one notes that the state via designated support funds and via underwriting of the banks' soft loan policies has been propping up loss making firms without any obvious sign that firms were doing anything other than waiting for demand to pick up in order to rectify their losses. Since the channelling of investment by the *chaebol*, with state support, into semiconductors, third generation mobile phone technology and computer chips had coincided with not only global recession but also global overproduction in these markets (consumers were finding for example that they didn't need a new computer every other year, or a chip that processes a nanosecond

faster than the one they had) it was not clear that this was a viable policy and South Korea's new and growing current account deficit and looming trade imbalance tend to indicate this.

Furthermore, growing unemployment (fluctuating between 4 and 5%) in a previously full-employment economy meant that in the meantime it has been the ordinary working and voting population that has been footing the bill through taxes that simply disappear into the black hole of debt and through lower wage growth and job losses. Not only have they been footing that bill it was also clear that there was a basic political conflict over who would bear the long term cost in terms of what economic restructuring would mean. From the late 1990s onwards, the political parties had begun to discuss labour and social welfare reforms to introduce a neoliberal style flexibilisation of work culture, based on easier hiring and firing, greater wage differentials, reduced bargaining with the newly independent unions, and later retirement ages. This seemed to cut to the very heart of the gains made by the populous out of not only economic development but the democracy movement of the 1980s that had forced the state and *chaebol* to pass on the economic benefits of growth. To be now made to foot the bill for the incompetence of government and management was beginning to seem like an additional and long-term insult.

Moreover the sense of dissatisfaction engendered was one compounded by the use of shell or holding companies to disguise business losses and siphon off state support funds. This in itself leads to pressure for the state to make full use of the powers and initiatives already enacted or proposed on personal ties and on corruption and graft. In 2001, for example, The Board of Audit and Inspection, found that \$5.67 billion had been

diverted from government bailout funds for the support of illiquid firms.

The Board has the authority to inspect abuses of public authority or misconduct by public officials in their official duties and audit the financial accounts of central and local government agencies, government corporations, and related organizations. It is responsible only to the president and is therefore reliant to some degree on the probity of the president and his commitment to clean government. With the scandals surrounding Kim and other politicians of all parties and the link between parties and the *chaebol* it was not obvious such probity could be relied on.

Roh's election, therefore, would seem to be a demand for accountability to become genuine, for change to be real, and for long term policy to value work but not exploit the worker. As in the Japanese case, since the reality of the problems listed are not only structural but tied into vested interests that cannot be easily swept away the apparent shift away from the strong state brings its own problems indicative of a political system in some kind of transition. Essentially, how does one remain elected and retain a mandate in the face of intransigent interests that knew enough to recognise the need for a sense of open politics but that will also resist genuine change that is potentially to their detriment?

Such is the challenge facing both Roh and the viability of the political system. It was immediately tested when in 2002 Roh was blocked by both the GNP and his own NMDP in making key appointments to The Board of Audit and Inspection. In October 2003 in the subsequent conflict Roh resigned from the NMDP and 37 young MPs defected to form the Our (*Uri*) Party. Roh, denounced as a traitor by his former party, thus faced a hostile National Assembly capable of blocking any policy initiatives, such as his

attempt to navigate labour reform in *New Vision for Industrial Peace* (2003).

In March 2004, the GNP-NMDP further tested the strength of Roh's mandate by taking the unprecedented act of impeaching him for an executive regulation infraction. At a press conference in February Roh had voiced support for the Uri Party in the forthcoming April National Assembly elections, breaching the required neutrality stipulation. Given the recent corruption scandals surrounding other politicians, the manipulation of this technical breach was an obvious attempt to sideline him – one that the media strongly supported (Roh was pursuing the major media firms for massive tax evasion). The Assembly voted 193 to 2 for impeachment with the Uri Party boycotting the vote in this “bloodless coup”. Amidst scenes of chaos and physical confrontations in the Assembly and a self-immolation protest outside, Roh was suspended pending a Constitutional Court hearing, with the prime minister taking over command of the armed forces, diplomacy and State Council meetings. As a result, even more so than the 2002 presidential election, the 2004 National Assembly elections became a litmus test for change versus the status quo – particularly when in late March, Park Chung Hee's daughter Park Geun Hye emerged as leader of the GNP.

The mandate for change, seemingly, was vindicated with the Uri Party increasing from 49 seats to 152, winning a slim majority position over the GNP with 121 seats and with the disgraced NMDP, despite strong media support, all but collapsing. As the Uri party leader, who had staged a hunger strike in support of Roh put it, “This election means that the old political forces that have dominated South Korean politics for 44 years are forced to leave the stage.” (Watts, 2004). This may well be premature, in the sense that relatively few new policies have yet to be

implemented under the new regime, but in terms of the message it sends to the political elite, it could not be more profound – a strong state can no longer be a domestically unresponsive state.

Interestingly, however, Roh's election indicates a different position vis-à-vis international pressure than that taken up by Japan. Whereas Japan, seems to be moving towards greater conformity to new American pressures for militarization, South Korea popular opinion seems to be moving increasingly away from the US (Lee, 2003). In 2001 Kim Dae Jung angered the American administration by affirming the Russian position that the 1972 Anti-ballistic Missile Treaty was the basis of strategic security, at a time when Bush was abjuring the treaty. Bush has also been consistently more hardline than the recent South Korean “sunshine policy” on North Korea, placing it within his “axis of evil” in his State of the Union address, January 2002, and reacting strongly to revelations that Kim Jung Il's regime had been using its small nuclear reactor in Yongbyon to manufacture enriched plutonium for nuclear weaponry in violation of the UN 1994 Agreed Framework (Rozman and Rozman, 2003). Though Roh has sent troops to Iraq as part of the US coalition, he is outspoken in that coalition in his criticism on the general strategy of the US in the “war on terror” and on North Korea in particular and wants a greater emphasis on concessions and aid in the periodic 6-way negotiations (China, North and South Korea, Japan, Russia and the US) in Beijing. This is despite:

- A North Korean strategy of attempting to increase its leverage by expelling International Atomic Energy Agency observers in 2002, and through the kidnapping of South Korean and Japanese citizens.
- Recent revelations from some of the 300,000 refugees in China that North



Korea is in the grip of a long-term widespread man-made famine and has been engaged in developing chemical weapons that it has tested on its own 200,000 political prisoner population.

- The April 2004 disclosure from the Pakistan scientist, Abdul Khan, who gave North Korea nuclear technology that it has viable nuclear weaponry already.

For South Korea, however, North Korea is more than a US security concern it is divided families and a divided people.

### 3. Taiwan

Even more so than in the case of South Korea Taiwan's divided nation status has shaped its relations with the US and world institutions. The full name of the island state of Taiwan is indicative of its unique international status. The name "The Republic of China on Taiwan" (ROC) is intended to emphasise Taiwan's claim to be the legitimate political power over mainland China. Though the ROC renounced this claim in 1991 its legacy still forms the basis of its relationship with the mainland and with the world at large. The claim has been reciprocated throughout by the Chinese Communist Party in the People's Republic of China (PRC). The PRC claims Taiwan as a renegade province. Whilst each side has claimed the other an uneasy truce has persisted on the basis of an assumption of long term reintegration. Reintegration remains the PRC policy though the ROC is now more ambivalent.

In 1954 the ROC signed a mutual security treaty with the US. However, in 1978, the US withdrew diplomatic recognition from the ROC (without fully renouncing its security commitment to it) and re-established diplomatic relations with the mainland in 1979. As nominally a province of the mainland, the ROC has an ambiguous status

in international relations since sovereignty conventions prevent part of a state being recognised and fully joining international institutions or actively engaging in diplomacy. Furthermore, any shift in policy away from the tacit assumption of long term reintegration towards strong claims of individual statehood is seen as a challenge to the status quo by the PRC and a local security problem by the US. For the US this exacerbates its long term difficult relation with the PRC - a state that has increasingly become important within the world economy and can now afford to modernise its military.

In terms of the strong state concept, the ROC shares with South Korea a post World War II history of military and effectively one-party authoritarian dictatorship. In 1949, facing defeat by the CCP in a civil war (1946-1949) the Chinese Nationalist Party (*Guomindang*, GMD), headed by President/General Jiang Jieshi (Chiang Kai-shek) retreated with one million refugees and a large portion of the mainland state's financial assets to Taiwan. The island had been recaptured from the Japanese in 1945 having been ceded in the Sino-Japanese war of 1895. A GMD emergency decree in 1948 placed the island under martial law, and, justified by a war footing against the CCP, provided the president with virtual unlimited powers to suppress political opposition. This executive power formed the basis of GMD domination of the political system until its repeal in 1986.

The political system itself was imported with the GMD mainland regime. The National Assembly, elected on the mainland in 1947 was not subject to direct re-election until 1991. Since the regime continued to claim rule of the mainland, it included political representation of the provinces on the mainland. Since the constituents of those provinces could not vote – representatives were elected in perpetuity for them, again

until 1991, when these representatives were retired.

From 1949 until his death in 1975 supreme power was exercised by President Jiang Jieshi. Upon his death he was succeeded by his son, the prime minister, Jiang Jingguo. Under both Jiang's the president was nominally elected by the National Assembly. The president is both head of state and of the armed forces. He appoints the premier who heads the cabinet (the Executive Yuan) which is responsible for policy, and exercises authority over the administrative branches (Yuan) of the political system that stand alongside the National Assembly, including the cabinet itself, and a Legislative Yuan. Where the National Assembly monitors the activities of the president, and amends the constitution and ratifies presidential appointments, the Legislative Yuan, serves to debate and enact law in much the way of any other parliament. Under both Jiang's all aspects of the political system tended to be "rubber stamp" institutions.

During this period of leadership continuity the ROC experienced rapid economic growth. By the mid-1990s the ROC was the 14<sup>th</sup> largest economy in the world and had successfully moved from agriculture, through cheap labour intensive forms of low-skilled production, into similar hi-tech markets to South Korea and Japan, as well as maintaining a foothold in processed foods and textiles. The ROC has actually had a larger public enterprise sector per capita than either South Korea or Japan. Firms controlled through the Ministry of Economic Affairs have dominated power production, primary extraction industries and heavy industry whilst the Ministry of Finance has controlled 4 of the major banks. However, unlike in Japan and South Korea, public-private relations based on conglomerates have not been the primary focus of economic

development. Employment (over 70%), exports (over 60%) and growth have been dominated by small private businesses employing between 10 and 300 people (Fields, 1995). These businesses tend to be highly paternalistic, family owned and run. They are typically integrated into larger loose quasi-organisations throughout East Asia and the world on the basis of complex networks of personal relations through which business is conducted and capital is raised.

In a formal sense, therefore, the state has played a lesser role in economic development (Wade, 1993) than in South Korea and Japan. The ROC does not seem to share with them the same basic problems of industrial structure and finance. The redistribution of land from large landowners to small farmers in the 1950s, compensated by stock in new state-owned industries provided some of the capital and incentive for the ROC's first generation of industrial capitalists. Much of the rest was provided by American market access and foreign direct investment in the 1960s and from the assets of politically and economically powerful families such as the Soongs and other "refugee" capitalists from the mainland.

The main formal role of the state has been to encourage exports, and to provide excellent infrastructure investment, including in education (Ashton, Green, James and Sung, 1999). However, given that ever since the GMD's ruthless expulsion of its left wing in 1927, the GMD has been dominated by industrial and financial capital, political and business interests have always been merged and many of the family owned businesses are operated by GMD members. Issues of client-patron relations, corruption (particularly public works contracts), graft, political influence and accountable open government have, much as they have in South Korea and Japan, therefore, become issues in ROC political discourse. The GMD itself has

interests in a wide variety of businesses and has assets in excess of Taiwanese \$50 billion.

Democratisation of the political system began under Jiang Jingguo and, it has been argued (Rigger, 1999), has similar roots as those in South Korea, in a combination of civil society changes, economic changes and a US-security relation shift with the winding down of the Cold War. Transformation has, however, been more stable, staged and incremental, involving less in the way of civil conflict. In 1986 local municipal elections were held and an opposition Democratic Progressive Party (DPP), comprised mainly of Taiwanese natives (distinguished from the 1949 refugees) was formed. Although it was not until the 1989 Civic Organizations Law that new political parties became formally legal. In 1988 President Jiang Jingguo died and Lee Denghui of the GMD succeeded him. In 1990 Lee was elected by the National Assembly to a 6 year term. In 1991 the National Assembly itself became subject to re-election in 4 year terms. Thereafter, the National Assembly took steps to democratise the Yuan and the constitution. Mainland MPs were retired, the Legislative Yuan was streamlined and members became subject to election for 3 year terms in 1992. In 1994, the constitution was amended to allow for direct election of the president. In 1996, Lee Denghui became the first president to be directly elected (for a four year term with 54% of the vote) and the GMD also maintained majorities in the National Assembly and the Legislative Yuan (Copper, 1998).

From a GMD perspective, the initial transition to democracy appeared remarkably successful. The Party remained in power. There were no major political scandals or economic problems on the scale of Japan or South Korea. Moreover, the GMD seemed to have dealt with two important issues. First, democratisation had been accompanied by an

apparently successful strategy of reconciling the “nativist” (*bentu*) and the refugee populations—a split which has been a longstanding socio-political problem. This appeared to be symbolically sealed in 1995 when President Lee, himself a Taiwanese native, formally apologised on behalf of the Party for GMD oppression—particularly the 2-28 *Incident* of 1947 in which an island-wide protest against the GMD government resulted in the brutal slaying of thousands of Taiwanese.

Second, relations with the PRC, though hardly friendly, were relatively stable on the basis of the 1992 “One China” agreement. Although the ROC had relinquished a claim on mainland sovereignty it was agreed that the status quo of “one China with different interpretations” (*yige Zhongguo gezi biaoshu*) would remain the basis of relations. On this basis, the ROC was able to apply for WTO membership as a special customs territory and was admitted into APEC as Chinese Taipei. Economic growth remained above 6% throughout the 1990s. Part of the reason for this was de facto integration with the PRC through increasing investment and trade links, initially mediated through Hong Kong. This “Greater China” link has proved extremely useful during the East Asian Financial Crisis because continued growth and investment in the PRC tended, initially at least, to drag the ROC along avoiding some of the demand problems faced by South Korea and Japan.

However, this relative success has also coincided with a growing political diversity that itself brings into question the insularity of the state in ways that relate to the ROCs relatively unique circumstances. A vote for the DPP seems to be a mandate for radical change. It seems to challenge the status quo in terms of GMD-refugee interests both politically and within the business community. The growth of the DPP is not a rejection of the integration strategy of the

GMD but it may be a radicalisation of it that reverses the presumed power relations of personnel within the state. The growth of nativist influence in ROC politics thus also carries the potential for further political fracture along quasi-ethnist lines.

It would be easy to overstate the significance of any schism based on the nativist-refugee division. The ROC has a population of approximately 23 million of which around 20 million are nativists, who mainly emigrated from the nearby mainland provinces of Fujian and Guangdong in the 18<sup>th</sup> and 19<sup>th</sup> centuries. The mainlanders or refugees arrived from all over China between 1945 and 1949 and constitute around 2 and a half million people, with the remainder made up of an indigenous aboriginal population. It follows, therefore that any GMD electoral success carries with it a large nativist vote. However, it does not follow that the same is true of the growth of the DPP. Fear of what this might mean resulted in the creation of the Chinese New Party (CNP) in 1993. The CNP was formed largely from second generation GMD refugees. Its platform both criticises the “Taiwanisation” of the GMD (and thus Lee’s prominence) and advocates a pre-1991 reunification policy.

The reprisal of a reunification policy highlights a further issue. Article 1 of the DPP party platform is to establish a sovereign and independent ROC. A vote for the DPP is, therefore, not just a nativist vote it is also a rejection of the whole refugee narrative with its claim on the mainland. Quasi-ethnicity has thus also complicated basic alternative foreign policies.

As the political system diversifies therefore, it faces a similar challenge to the South Korean system. Where South Korean politics struggles with ambiguous political philosophies and regional factionalism the ROC confronts a basic identity problem between different generations of Chinese

migrants. What it will mean to be Taiwanese has become part of political choice. Since the GMD, now contains nativist politicians and seeks election from a predominantly nativist population, it cannot dismiss the pull of a single sovereign Taiwan. Thus, in 1999, Lee Denghui, was prepared to unsettle the US, the PRC, the breakaway CNP and many within the GMD, by raising the possibility of a two state solution to the PRC-ROC relation in the run-up to the 2000 presidential election. It wasn’t enough to secure a GMD victory, however, and for the first time since the founding of the ROC, the GMD lost control of central government.

The 2000 presidential election was won by the DPP leader, Chen Shuibian, with just 39% of the vote. President Lee’s nominee for the presidency was vice-president Lien Chan. Chan defeated the GMD governor of Taiwan, James Soong, for the GMD candidacy. Soong chose to stand as an independent and came in second with 37% compared to Chan’s 23%. One major reason for the DPP victory, therefore, lies with a debilitating split within the GMD. Just as important, however, was the DPP’s “Resolution on the Future of Taiwan” in which the Party restructured the semantics (but not the substance) of its emphasis on a sovereign ROC to make it more compatible with the status quo and less confrontational to the PRC. This is important because whatever the political issues of independence may be, economic interdependence grows by the year. By the beginning of 2004, 1 in 20 Taiwanese was living and working in China and China had become the ROCs major trading partner despite quotidian obstructions on either side. The DPP’s semantic adjustment on the two China’s issue was, therefore, significant because it allowed the case to be made that Chen could be trusted to manage cross-strait affairs with the PRC.

Chen's election shares a number of features with that of Roh in South Korea. In terms of policy the DPP manifesto challenged the business interests and corporate links of the GMD by combining pro-environmentalism (such as opposing the expansion of nuclear power production on the island) and a greater emphasis on workers rights and welfare issues. Chen was also immediately confronted by a hostile Legislative dominated by the GMD. In a similar fashion to Roh's circumstances, events were to make the next Legislative Yuan election a test for change versus the status quo.

As a result of the GMD failure in the presidential election the GMD sought to redefine itself further towards the CNP. As a nativist with leanings towards an independent ROC, Lee Denghui felt obliged to resign as chairman of the GMD. At the same time, James Soong formed the People First Party (*Qinmindang*, PFP) creating a right or "pan-Blue" bloc with the GMD and CNP. Lee then formed the nativist Taiwan Solidarity Union (TSU) Party creating an opposing "pan-Green" bloc with the DPP. This sharpening of political positions along identity lines was accompanied by political stalemate as the Legislative Yuan sought to block any policy proposals from Chen, and also by recession as business investment sharply reduced, the stock market fell and unemployment rose on the basis of the sudden sense of uncertainty, following years of pro-business stability under the GMD. Despite this recession, the GMD lost 55 seats in the Legislative election of 2001 and the DPP-TSU increased its share to 100 of 225 possible seats allowing it to form a minority government.

Accountability, increased choice and greater democratic participation have, therefore, been accompanied by an increase in factionalism, political conflict and economic problems in the ROC. The strong

state seems to be becoming the volatile state. The recent 2004 presidential election has served only to highlight this. The pan-Blue bloc stood Lien Chan as their candidate against Chen with James Soong as vice-president. The election was characterised by South Korean style bitter personal attacks in the media and an assassination attempt on President Chen, which the GMD then claimed was a DPP plot to garner a sympathy vote. Chan won the election by a 0.2% margin or just under 30,000 votes, but according to the Central Election Commission over 300,000 votes were discounted as "spoiled" raising a similar legitimacy spectre to that which haunted the election of George Bush.

#### **4. Conclusion**

§1-3 suggest that Japan, South Korea and Taiwan have shared a number of common features. During their periods of greatest economic growth all 3 were governed by forms of authoritarian political systems associated with a degree of closure and policy continuity which commentators have used to explain the success of their economies in terms of a concept of the strong state. In the case of Japan and South Korea this has also been linked to the concept of an interventionist developmental state. In all three cases aspects of that authoritarianism have been linked to their relation with the US and the role of the US in the Cold War. Subsequently, each of the 3 has undergone a degree democratisation. In the case of Taiwan and South Korea that democratisation has been initially one of formal systemic reconstruction. In all 3 cases, however, it has also been one of the diversification of political choice, practice and personnel. In all 3 cases accountability seems to be conjoined with, in some sense, a reduction in political longevity, producing both problems and opportunities. In either case, the increasing diversity of the 3 state's political systems

would seem to bring into question the continued adequacy of the strong state concept in analysing them. As the 21<sup>st</sup> century proceeds East Asia seems therefore to be in the early stages of epochal change.

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## Objectives of Government Policy

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### **Introduction**

In general terms, the term “applied economics” implies the application of several measures by policy makers to achieve some objectives. In this sense, the policy maker must take into account not only the economic analysis (theory, models...), but also the economic facts (information data, historical facts...) and value judgements (preferences). Considering all these aspects, some policy recommendations are given and finally the economic policy measures are adopted. In order to design economic policy measures it is necessary to consider the relationship between objectives and instruments (Bronfenbrenner 1963).

The main objective of this article is to analyse the role and characteristics of the objectives of government policy. We will start delimiting the concept of objectives in political economy and we will present a general classification of objectives. We will also study the main objectives, taking into account the main instruments that the policy makers could use to achieve them. Later we will consider the non-compatibility among objectives and we will finish considering the main conclusions.

### **Definition of Objectives**

When the economic behaviour is analysed it is necessary to take into account that society would like to achieve some general and broad objectives that would include the motivations and general purposes. These general objectives have a constitutional base and are desired by the most of individuals, e.g. equality, liberty... Therefore, there is a general consensus in order to achieve these general objectives and they are base to develop not only the economic activity but

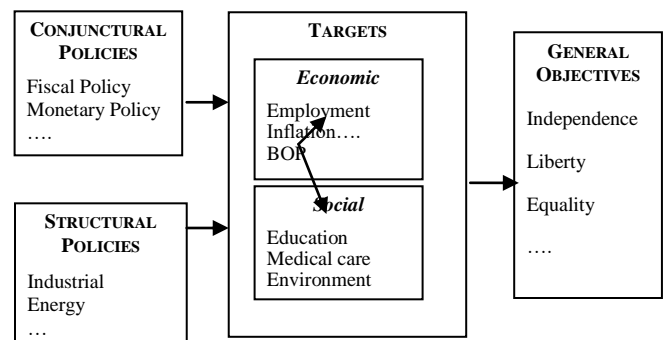
also the relationships among economic agents.

Together these objectives there are also other more concrete that are considered as targets to be achieved to obtain the general objectives. In this case, it is necessary a concrete definition, delimitation and quantification of these objectives. Two types of objectives can be considered. The first are economic objectives; that are inherently linked to general economic welfare, e.g. economic growth or prices stability. The second are social objectives; that is, those objectives that are not properly economics but facilitate to obtain a certain social welfare and important resources are necessary to achieve them, e.g., education, medical care, environment, and so on. Some of the social objectives are increasingly being seen as economic as well; especially in relation to the environment. This is dealt with in other articles in this present work.

To achieve economic and social objectives it is necessary to use adequate instruments or policies that could have effects on the cycle and/or the structure of the country. In this article we will consider the economic objectives and in some cases we will also take into account the main policies to achieve them

Figure 1 shows the relationship between these different objectives, targets and policies:

*Figure 1: Relationship Between Objectives*





## Classification of Objectives

A general classification of the economic objectives is shown in Table 1. In this table we have considered the objectives, the advantages obtained by the society if the objective is achieved and the main instruments that the policy maker could use to achieve the objective.

As it is shown in Table 1, six general objectives groups can be considered. The two first objectives could be included in the micro field and the main purpose is trying to reduce or eliminate the possible market failures that could exist. The other four objectives could be included in the macro area and they considered different problems that have negative effects on economic agents' behaviour from business cycles and on structural perspectives.

Following Table 1 we analyse the main objectives of government economic policy. We will start considering the micro ones and latter we will consider the other groups in an independent fashion.

*Table 1: Main Objectives of Policy*

Objectives	Advantages	Main Instruments
Increase competitiveness	Reduce prices Positive effects on economic growth The system is more efficient Technological progress is favoured	Prices control Industrial policy
Reduce monopolies	Improve system efficiency Reduce prices Increase technological efficiency Technological progress is favoured	Tax policy Legal system to control mergers
Economic Growth	Improve social welfare Positive effects on labour market	Technological policy Education Tax Policy
Income distribution	Positive effect on economic growth Reduce social conflicts	Tax Policy Income policy
Other objectives related to business cycles	Reduce economic disequilibrium (unemployment, inflation...)	Fiscal and monetary policies.
Structural objectives	Increase the flexibility and efficiency of markets	Industrial policies Structural reforms

## 1. Micro Objectives

As it was shown in the previous section, micro objectives try to eliminate the market failures when they try to achieve social efficiency. As Sloman (1991, p. 421) states, part of the problem is the lack of perfect competition, part is the existence of externalities and finally part is the difficulty that markets have sometimes to adjust to any disequilibrium given.

However, not only the difficult to achieve social efficiency is the problem. Markets also sometimes fail to obtain more general and macro objectives, e.g. equity, full employment, prices stability... For this reason, some economic literature states that government intervention is necessary and must try to reduce the market rigidities and increase competitiveness. And one way to get them is reducing monopoly activities.

When markets are imperfect, among other things there are two negative effects on society. First, the Pareto optimality is not achieved. This implies that Marginal Social Benefit is not equal to Marginal Cost to Society. Second, the consumer surplus is reduced and the producer's gain has been more than offset by the consumer's loss.

Therefore, when market is imperfect there is a welfare loss. However, this statement could be relaxed if we consider two situations. First, firms are interested not only in profit maximization. In this case, they may produce more than the profit maximizing output. Second, there are sometimes social advantages from large and powerful firms. They have more possibility to compete to other foreign firms, maintaining activity and work places.

On the second micro objective, increase competitiveness, it has similar characteristics to the reduction of monopoly. Higher competitiveness, increase consumer surplus and thanks to trade activity facilitate the introduction of new technologies that will reduce prices.

## 2. Economic Growth

During the last decades, economic growth and its causes have been considered as the most important questions in economics: “economic growth has become the secular religion of advancing industrial societies” (Bell 1976:237).

On the definition of economic growth, Kutznets (1966:1) offered a simple one: growth “is a sustained increase in per capita or per worker product”. Therefore, in general terms, economic growth is the increase in the value of goods and services produced by an economy during a period. It is relevant to distinguish between actual and potential growth (Sloman 1991:472-473). Actual growth is the percentage annual increase in national output. Potential growth is the speed at which the economy could grow, if all the resources are used. The distinction between both concepts is important to analyse the causes of economic growth.

For empirical purposes economic growth is generally measured as a percent rate of increase of gross domestic product (GDP). Considering this variable, it is supposed that economic growth is an increase in the wealth of a country, referring to growth of potential output. Growth is generally calculated in real terms, in order to eliminate the effect of inflation on the price of the goods and services produced during the period considered, being an indicator of the average standard of living of individuals in a country. Depending on the data availability other variables have been also considered (per worker GDP, productivity...).

From the theoretical point of view, many economists consider that the main reason of the economic growth relevance for policy makers is due to the fact that it implies higher prosperity (e.g. Layard 1997). Therefore, from this perspective economic growth is considered as one of the ultimate measures of

a country well-being, due to the beneficial effects on other economic policy objectives such as employment and the production of goods and services. Both are considered as relevant parts of the individuals’ welfare. But economic growth also facilitates the achievement of other objectives (for instance improvement of income distribution, reducing the inequality) that have also a positive impact on individuals’ happiness

For all these reasons policy makers are especially worried on this economic policy objective. Nowadays, countries usually rate the competence or incompetence of the government activity in terms of economic growth. From their point of view, higher economic growth rates imply an adequate economic policy and are cause of national pride, having more possibilities to be re-elected in future political elections. So, those countries that achieve lower economic growth must change their policy strategy and they have to follow and to copy the policies designed by the higher economic growth countries.

This traditional vision has been improved considering other aspects related to economic growth such as the opportunity to use resources in an adequately way and to achieve a sustainable prosperity for the individuals (McMahon and Squire 2003).

However, economic growth doesn’t show only positive effects and it is also necessary to take into account the negative ones. In general terms, the main positive and negative effects caused by economic growth are:

1. Level of employment. As it was stated before, economic growth maintains or improves work places. Following the Keynesian point of view this result is due to higher levels of consumption as consequence of the increase of income per capita that encourages production activity.

2. However, economic growth also implies rapid changes in the production process,

introducing new technologies. If people cannot improve their skills, their jobs may be replaced by machines.

3. Income distribution. If incomes rise government has the possibility to favor poor shifting incomes from the rich to the poor. However, several mechanisms could have some influence in this relationship that will be considered in the next point.

4. Macroeconomic difficulties. Higher income would lead to a higher demand that could generate inflation and balance of payment problems due to the increase of imports of goods. Thanks to an increase of production all these problems could be avoided satisfying the individual's necessities.

5. Environmental resources. The relationship between economic growth and environment is not clear (Selden and Song, 1994, Magnani, 2000, Andreoni and Levinson, 2001, Heerink et al., 2001, Eriksson and Persson, 2003). Some literature states that as individuals are richer they are more preoccupied with the environment. Higher education facilitates this process. However, economic growth would use greater amount of resources, some of them non-renewable. In this case, improvement of scientific knowledge is necessary to avoid this problem. On the other hand, higher consumption derived from the economic growth generates higher level of pollution and waste.

6. Welfare and happiness. From the previous points can be concluded that avoiding some costs (mainly distribution and environmental problems) economic growth drives to a higher society welfare and finally to a higher happiness. However, some controversies have been developed in this field. Ethical claims have appeared recently stating that "the more people have, the more they want" and for this reason more consumption may not increase their utility. It

will only lead the individuals to a material society, more selfish and less caring society. This society may thus become more unstable with higher rates of crime, divorce, suicide and so on (Friedman 2005). Thus 'happiness' has become an interesting area of analysis (Frey and Stutzer 2002, Easterlin 2005).

### **3. Income Distribution**

Income distribution is concerned not only with economics but also ethics. For that reason, this objective can be studied in different ways and considering different relations and effects on other economic policy objectives, especially economic growth. In this sense, the empirical and theoretical studies have reached different conclusions about the relationship between income distribution and growth.

In this sense, during last century economists started to be interested in such relationship since the publication of Keynes (1936). Considering the hypothesis that the savings is related to income, during the 1950s and 1960s some economists (Kaldor 1956, for instance) stated that it would be necessary to redistribute income to richer persons, who have a higher propensity to save than the poor, thus increasing capital accumulation and economic growth.

During those years, the Kuznets curve was introduced. This "inverted-U" hypothesis, suggested that economic growth can initially lead to a rise and then fall in income distribution within a country. Since then, empirical studies have tried to test this hypothesis, many of them not finding confirmation of the "inverted-U" curve.

Income distribution has also effects on economic growth. Economists have not had a unanimous position on the sign of this relationship. In the literature of the 1950s and 1960s it was accepted that higher inequality would enhance economic growth (e.g. Kaldor, 1956; Kelly and Williamson, 1968;

Cook, 1995). They considered the hypothesis that the savings is related to income and play a relevant role in the economic growth process. This implied to use a redistribute fiscal policy that shifts income from poorer to richer, who have a higher propensity to save.

This view has been criticised and changed during the last decades. The empirical literature showed from this new position that could be a negative relationship between inequality and economic growth (Kuznets 1955, Galor & Zeira 1993, Persson & Tabellini 1994, Bénabou 1996, Alesina & Perotti 1996, Aghion et al. 1997, Zou & Li 2000, Alfranca & Galindo 2006). Different channels could explain this new view (Perotti 1996:150-154; Aghion et al 1999:1621-1630):

a. Fiscal channel. In an unequal society, poor voters are likely to vote for those fiscal programs that promise a better income distribution through taxation or public expenditure. That implies the fiscal redistribution must be financed by distortionary taxation that distorts economic decisions, and discourages investment and finally economic growth (Alesina & Rodrick 1994; Bertola 1993. On the public capital effects, see Alfranca & Galindo 2003).

b. Socio-political problem. Some literature (Alesina & Perotti 1996; Benabou 1996a,b) has stressed the impact of income inequality on political instability and social tensions. These problems will increase uncertainty that leads to a lower investment and economic growth.

c. Education (Becker et al 1990, Saint-Paul & Verdier 1993, Sylwester 2000). The empirical evidence shows that there is a positive effect of education on economic growth. In the case of income inequality, higher inequality implies higher underinvestment in the education when credit markets are imperfect.

d. There are also other channels that consider the relationship between income distribution and growth, including democratization (Bourguignon & Verdier, 2000), property rights (Svensson 1998; Keefer & Knack, 2000), economic volatility (Alesina & Perotti, 1996; Aghion et al 1997), among others.

#### **4. Other Objectives**

In this section we will consider other objectives, which main goal is try to regulate business cycle, reducing economics disequilibrium. The most relevant objectives to be included in this group are:

##### *a. Unemployment*

This is the macroeconomic problem that affects individuals most severely and directly. There are several costs of unemployment, not only economic. The most obvious is the loss of money (salary) and the difficulties to attend the family necessities. However, there are also other economics costs related to the reduction of output, the underutilization of resources and the government lost tax revenues and the increase of employment subsidies. There are also non-economic costs, psychological, reduce of self-esteem and the possibility to succumb to stress illness and social, unemployment leads to increase crime.

For all these reasons unemployment is a frequent topic of political debate and many politicians use employment data to obtain more votes. Sometimes the “misery index” (the sum of inflation and unemployment rates) is used to measure the health of the economy (Mankiw, 1994, p. 118) and this index and economic growth rate are the main indicators of the success or failure of the economic policy designed by the policy maker.

Several types of unemployment may be considered and the policy maker must be to take into account them during the process of the design of the policies. The main types are

(see e.g. Dornbusch and Fischer, 1988, Sloman, 1991, Sapsford and Tzannatos, 1993, Mankiw, 1994):

From this point of view the cause of unemployment is that real wages are above the market-clearing level. This possibility may be due to several circumstances. First, the trade unions use their power to increase wages. Second, the minimum wage legislation introduced by the government states a minimum wage above the market-clearing level.

From this perspective, obviously the solution to the problem is to reduce the real wage. However some problems and difficulties appear. First, the reduction of minimum wage affects negatively to the poorest individuals. Second, the reduction of average real wages will also reduce the consumption expenditure have negative effects on demand for labour. And finally, it is quite difficult to reduce the power of unions to push up wages.

Keynesian unemployment or demand deficient unemployment.

In this case, the unemployment is associated to an insufficient demand characteristic of economic recession periods. During these periods, the consume expenditure consumption falls and appears stocks in the firms because they are not able to sell all their products. Therefore, they reduce their production activity and the demand for labour.

This kind of unemployment may exist not only cyclically but also at long term if the economy is situated constantly below full capacity and labour market continue at disequilibrium.

From this perspective, the government may reduce unemployment rate increasing or assuring a high aggregate demand. Public expenditure or reducing taxes will increase the aggregate demand. However, they will also have negative effects on inflation and

balance of payments that reduce competitiveness and could have future negative effects on production and employment.

Frictional unemployment. This is the situation when individuals leave their jobs and spend some time looking for a new job. This kind of unemployment is mainly voluntary and usually the workers don't accept the first job they are offered hoping that a better one will turn up. To reduce this kind of employment there are at least two remedies. First, improve the job information. Government job centres and private employment agencies play a relevant role in this field. Second and more controversial remedy is that government reduces employment benefit.

Seasonal unemployment. It occurs when the firms' activity is affected by the seasons of the year. This is the case of tourism activity. During the holidays more jobs are offered and they are reduced in the rest of the year. Government could reduce this kind of unemployment introducing demand policies, for example, trying to modify holidays habits (individuals spend their holidays in different periods of time, not only during July or August) and giving subsidies to retirement to spend days in tourism areas during the non habitual holidays days (e.g. during October, November, etc).

Structural unemployment. It appears when there are important structural changes in the economy. Depending on the cause of the changes the firms would be affected in a different way. For example, if there is a change in the methods of production, those enterprises that introduce new technology could need fewer workers for the same level of output. If there is a change in the pattern of demand, that is, there is a change in the consumer tastes, those firms that produce goods or services not desirable will reduce the level of output and the number of

workers. In this case, government intervention is possible introducing demand and supply oriented measures. Demand side policies imply that government maintain the demand level, reducing for example taxes. And the supply oriented policies imply that some subsidies and grant are offered to firms to introduce new technologies or to improve their production methods and processes.

### b. Inflation

If unemployment is considered mainly as an individual problem, inflation is viewed as a social problem. As Mankiw (1994, p. 140) states “in the 1970s President Gerald Ford declared inflation “public enemy number one” and in the 1980s President Ronald Reagan called inflation “the cruellest tax””. The reason for these negative statements on inflation is due to the cost derived from it. First, inflation generates uncertainty among entrepreneurs, because they have difficulties to predict revenues and costs. Therefore, the incentives to invest are reduced having a negative effect on economic growth. Second, inflation worsens the balance of commerce, because the domestic products are more expensive. Hence exports will fall while imports rise. In this process the exchange rate will also be affected. Third, inflation causes a redistribution of income between those individuals that have not possibilities to defend their situation (mainly individuals with fixed incomes) and those individuals that can defend their position (basically those that receive profits or rents). This redistribution could affect negatively on economic growth as we examined in a previous section of this article.

There are different theories on inflation (see e. g. Dornbusch and Fischer, 1988, Sloman, 1991, Mankiw, 1994). Some of the more generic ones are discussed below.

**Money.** Monetarists state that inflation is a monetary phenomenon. Therefore, the best

way to cure for inflation is that the government controls the supply of money in the economy.

**Demand-pull inflation.** In this case, increases in the demand cause inflation. Higher demand could be caused by lower interest rate and tax rate, higher government expenditure increase demand and an improvement of the entrepreneurs’ confidence that would increase investment.

**Cost-push inflation.** This inflation is caused when cost of production rise. There are several possibilities: a rise of the wages, of the price of raw materials... In this case, firms have to face to an increase of the costs and they respond passing the higher costs to the consumers, increasing the prices and partly reducing production.

As can be seen from Figures 2a and 2b, demand-pull and cost-push inflation are caused by different things and have different implications for the economy. Demand-pull (Figure 2a) inflation is caused by a rightward shift of the aggregate demand curve (AD<sub>1</sub> to AD<sub>2</sub>) increasing prices and output (Y<sub>1</sub> to Y<sub>2</sub>). Cost-push inflation (Figure 2b) is caused by a leftward shift of the aggregate supply curve (AS<sub>1</sub> to AS<sub>2</sub>), increasing prices and reducing output (Y<sub>1</sub> to Y<sub>2</sub>). While they have a similar impact on prices, their impact on income and employment are opposite.

Figure 2a: Demand Pull Inflation

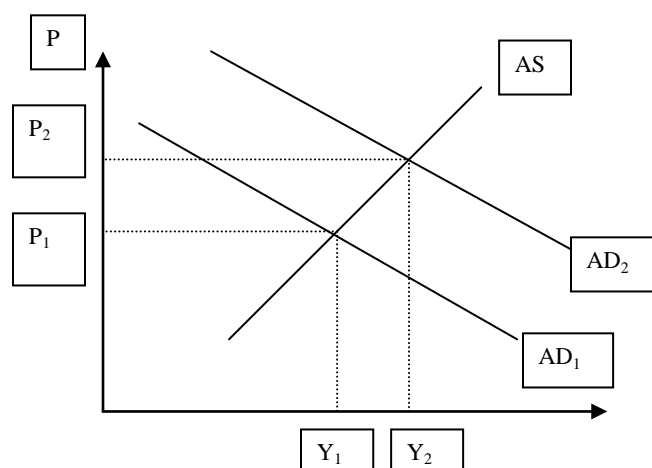
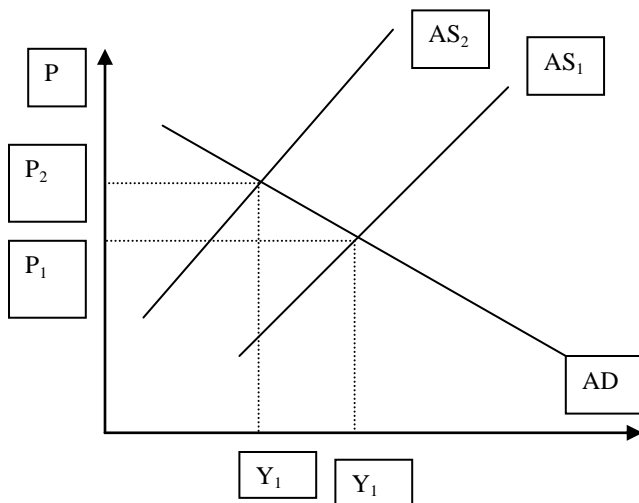
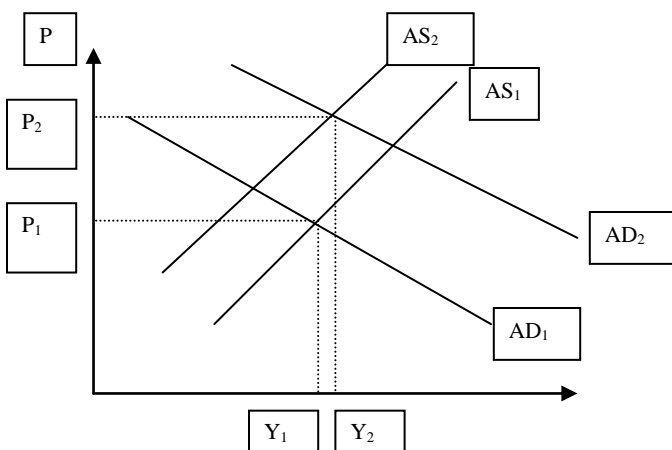


Figure 2b: Cost-Push Inflation



It is important to recognise that both types of inflation can occur together, as shown in Figure 3, below. An increase of wages could encourage to government to increase the expand aggregate demand and avoid the negative consequences on unemployment. In this case, usually is quite difficult to separate the two. While the effect on prices is quite easy to see, it is not easy in the case of output. It will depend on the nature of the shifts of both curves.

Figure 3: Demand-Pull and Cost-Push Inflation



One problem derived from this situation is the possibility that a wage-price spiral might appear. With higher prices, trade unions will demand higher wages to maintain the cost of

living. In this situation entrepreneurs will increase again the prices and trade unions will ask higher salaries and the process follow increasing wages and prices. The situation could worsen if government tries to reduce the negative effects on labour market increasing demand or issuing more money.

Taking into account the types of inflation, two broad policies can be considered to reduce inflation. First supply policies that must try to maintain costs, e.g. increasing competitiveness, reducing monopoly practices, introducing income policies to maintain wages and profits and policies to increase productivity, among others.

Second demand policies that can be developed by fiscal and monetary policies. Fiscal policy must try to maintain and control public expenditure (or avoid taxes reductions) avoiding non desirable inflationary aggregate demand increases. Monetary policy would have to control money supply and to manipulate interest rate.

#### *Balance of payments equilibrium*

Finally, other objective to be included in this group is the equilibrium of balance of payments to avoid the negative effects derived form a deficit (e. g. higher unemployment) or a superavit (e. g. inflation). From a neoclassical point of view, it is not necessary the government intervention to achieve this objective, because it automatically balance. However, government in order to achieve the equilibrium could use exchange rate policies.

### **5. Structural Government Objectives**

If we take into account the structural policy, the main objectives to achieve by the government are (OECD, 1989, de Long and Summers, 1992, OECD, 1996):

- To improve the markets flexibility, trying to increase the productivity and to incentive

demand for labour, having positive effects on economic growth and employment.

- To contribute to the adequate market of goods and services working, guaranteeing the property rights and not distorting the signals issued by economic agents.
- To improve the efficiency of resources allocation.
- To enhance economic growth favouring the introduction of new technologies and production processes.
- To reduce or to eliminate trade barriers.

### **Compatibility Among Objectives**

One of the most relevant problems in the design of economy policy is the non compatibility among objectives. This non compatibility affects on the relationship between objectives and instruments, constraining the use of some instruments. For example, higher public expenditure would have positive effects on employment. However, would also increase prices that would reduce competitiveness and would have negative effects on demand for labour.

When this non-compatibility is considered, four aspects must be taken into account. The first is the non compatibility among objectives is due to the instruments used, not to the own objectives. As it is shown in the previous example, policy maker could try to achieve a certain levels of employment and of inflation. However, the use of the instrument, in this case the fiscal policy, creates the non compatibility or the negative effects on one objective.

The second is that sometimes the election of an objective depends on its independent character. Taking into account again our example, if we consider that employment depends on inflation behaviour, then the primary objective that must be chosen is inflation, considering that when inflation is reduced employment will increase.

The third is that incompatibility among objectives is usually impossible to avoid. To some degree the choices of trade-offs between objectives depend on value judgements.

The fourth is that this non-compatibility depends also on other non economic variables and behaviours, such as time lags, lack of information, social relevance, political cycle, and so on. Considering again the relationship between inflation and unemployment, if there is more information about prices, economic agents are more sensible to prices..., inflation will be then the objective chosen by the policy maker.

### **Conclusion**

In the previous sections we have considered the most relevant economic objectives that policy makers try to achieve in the developed countries. The election of the objective and the instrument is relevant to obtain adequate results and to obtain the necessary votes.

The main problem in the analysis is the existence of non-compatibility among objectives. In this case, the functional relation between instruments and objectives is affected, reducing its efficiency. This difficulty is mainly resolved from a political point of view. Economic sensibility and the political cycle will affect to policy maker decision. If individuals are more interested or affected by unemployment changes and the elections are closed, policy makers will chose to reduce unemployment as the main objective and probably fiscal policies to enhance aggregate demand would be designed (presumably higher public expenditure and/or tax reduction). The main problem of this behaviour is the future negative effects on other objectives.

Finally, it is necessary to take into account that other economic and non-economic objectives could be considered, especially in less developed countries, for example,



poverty, rule of law, and policies to reduce corruption. Most of these factors try to contribute to the achievement of some objectives that we have analysed in the previous sections. For this reason they have not been included in this article. Increasingly, though, some of our non-economic objectives are being seen as economic; or at least to all policy. This is especially the case for the environment and climate change, which is dealt with in other articles in this present work.

### Internet sites

International Monetary Fund. [www.imf.org/](http://www.imf.org/)  
 OECD. [www.oecd.org](http://www.oecd.org)  
 World Bank. [econ.worldbank.org/](http://econ.worldbank.org/)

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## Performance Based Budgeting

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### **Introduction**

In a search for government efficiency, a number of initiatives were introduced, on a regular basis, at the end of World War Two. From time to time, the government attempted to improve the way public money was allocated together with the control of commitments and results achieved by the programmes publicly funded. The state sector recorded significant growth, both in size and scope, throughout the 20<sup>th</sup> century, but especially during the post World War Two era. Taxation has grown (now taking up to 30 to 60 per cent of an individual's income) in order to fund an increased state and the government budget has grown in line with these newly acquired responsibilities. The more complex organisations were more difficult to control and the issues of accountability and effectiveness of control and oversight have been raised. In the 1970s, the concept of overload was created (King 1975), although in the 1960s there were numerous discussions about the credibility of the government institutions of the time and the need to devise new tools of governing and managing the public sector (Thomas 1968, Crick 1968). The debate was confined to the developed countries, while developing economies were to wait a further 25 to 30 years to initiate similar discussions (Verheijen & Coombes 1998).

Linking budgeting and performance has been just one of a number of attempts to address the issue of distribution of a shrinking public purse, especially by the defence departments. Attempts were made to link programmes and activities associated with those programmes with budgetary appropriations, in order to justify the spending allocations. These were made to

address the usual deficiencies of the traditional approach to budgeting, which assumed an incremental increase to budgetary items - budgets being prepared on a line-item basis. In a traditional model the government department will propose a line increase in their budgets, usually taking into account only inflation, where any extraordinary growth in funding will be the result of political compromise and relative political power and due to the prestige of the minister heading the respective government department. Ministers are perceived to be more important and their portfolios more prestigious if they control a larger part of the overall government budget and employ more public (or civil) servants. Downsizing the government department has generally become the fashion with the introduction of the New Public Management doctrine(s) in the 1980s (Hood 1991). Performance budgeting, planning, programming and budgeting (systems) have been just some of the responses given by accountants to the challenges of the public sector reform in the post World War Two developments (Lane 1995). Performance based budgeting systems, especially the traditional PPBS (Programme Planning Budgeting Systems), has traditionally been advised to less-developed economies, but from the very beginning there were some concerns about this practice (Caiden & Wildavsky 1974). But, despite this general unease with the model, a number of developing countries experimented with them long after developed countries ceased to use them in orthodox forms (Dean 1986).

### **Historical Developments in the Anglo-American Context**

The first applications of novel budgeting techniques that incorporated strategic information happened in the US in the 1960s. The US Department of Defence introduced a planning, programming and budgeting (PPB)

system in 1961. The system was both devised and (partially) implemented by Charles Hitch, in order to ensure centralism of implementation of the system, that was set up to focus on the effective use of resources. The post World War Two US defence budget has been constantly increased. It has been necessary to ensure that resources are allocated to the best possible uses, when all branches of the armed services have constantly requested new systems, as sophisticated as possible, which of course, is reflected in runaway procurement costs (see Hitch 1965). The implementation of the 'new' model was strongly supported by the then US Secretary of Defence, Robert McNamara, who seized the opportunity to utilise the better instrument of control and decision-making. After a few years of implementation within the US Department of Defence, PPB was adopted across the US Federal Government. The system that the US federal agencies employed in the mid-1960s was originally known as 'output budgeting', becoming known by its current name somewhat later, in the 1970s. However, there are, in fact, claims that experimenting with performance and programme budgeting dates back to the 1920s or even earlier, when US manufacturing companies (predominantly military suppliers) tried to link results and inputs (Novick 1973a). However, it is generally agreed that PPB is a child of the 1960s (Wildavsky 1979).

The PPB system initially had the objectives, as put by Schultze (1968): 1) to define the policy objectives in all major areas of government; 2) to organise information about expenditure and use of resources in terms of the specific programmes designed to achieve these objectives; 3) to analyse the output of programmes so as to have some measurement of their effectiveness; 4) to evaluate alternative ways of achieving the same policy objectives, incurring the least

costs, and 5) to formulate objectives and programmes for a prolonged period of time and to provide the feedback on the effectiveness and quality of the chosen methods (Schultze 1968, pp. 19-23). PPB was seen as the product of 'managerial rationalism' (see Challis *et al.* 1988), an instrument for planning government activities more rationally and emphasising efficiency and effectiveness. Schick (1969) favoured 'rational planning' rather than 'rational politics' as process politics was to favour partisans, whilst planning should take into consideration a broader picture, focusing on outcomes. In fact, the systems approach was designed with a focus on examining the outcomes (Schick 1969). Although it has been claimed that PPB has enabled the inclusion of 'disfranchised groups' views and interests into the public policy processes, it also, due to the need for higher centralisation for the implementation of the model, strengthened the powers of the executive, especially the US President. Consequently, the systems' models favour the centre, especially the top executive and the body in charge of organising and overseeing the budgetary process.

By the end of the 1960s the popularity of PPB had been declining, severely criticised by both professionals and academics, particularly the pluralists (see, e.g., Wildavsky 1979). However, the continuity of applications of innovations in the US has always been politically biased. It is very rare that the new administrations continue implementing initiatives launched by the previous administration, even if the presidents belong to the same party. It seems that the trend may change in the future, as the George W. Bush administration continued with the implementation of performance measurement initiatives launched by the Clinton administration in the early 1990s. This is an even more remarkable achievement, as the

implementation of the performance measurement and government reform programme was overseen by President Clinton's Vice President, Al Gore, who contested the Presidency with George W. Bush in 2000.

As the interest in PPB faded away in the US, the model attracted the attention of other countries over the Atlantic. The British Ministry of Defence initiated, in 1964, a system similar to the American 'output budgeting' in order to ensure the effectiveness and efficiency of defence procurements. In the late 1960s, Her Majesty's Treasury experimented with 'output budgeting' and encouraged other UK government departments to test this model. The Department of Education and Science commissioned in the late 1960s and published in 1970 (DES 1970) a feasibility study on the applications of PPB in the education and science portfolios. It emerged that PPB failed to attract wider attention, although other government departments (Department of Health and Social Security) "flirted" with the model in the mid-1970s, again with little success (Banks 1979). By the late 1970s when Margaret Thatcher took over as the British Prime Minister, the PPB episode in the UK was, more or less over, despite its fairly enthusiastic beginning (Klein 1972). In the 1970s it proved to be very difficult to translate 'output budgeting' into a more operational system, especially grasping the success indicators when the objectives are broken down into programme elements.

However, this did not mean that the British Government abandoned the idea of measuring and evaluating performance. PPB was replaced (if ever it was really endorsed in Britain) by the Programme Analysis and Review (PAR), to again disappear by the mid-late 1970s. After all these experiments, the Thatcher Government had its own review and evaluation agenda, put forward by the

Financial Management Initiative (FMI). FMI was not a simple performance budgeting model, but had a much broader view to include strategic and other variables in the budgeting process and using accounting information for better quality governance. FMI, launched in 1982, was one of the *early attempts* to introduce a wide range of changes in the British Civil Service. Before FMI, the British tried to improve the quality of Civil Service through the Fulton Report in 1968 and 'Efficiency Scrutinies' in 1982.

The FMI was further followed by the 'Next Steps Initiative' in 1988, the Citizen's Charter in 1991, Competing for Quality in 1991, Services First in 1997 and Best Value in 1998 etc. Since the launch of FMI in 1982, the British Civil Service has been subjected to a continuous process of change and improvement, to a large extent mirroring the changes experienced outside the Public Sector, not only in the UK, but also overseas. Although the goals were outreaching, and mainly 'non-financial' ('better value for money', 'downsizing', 'delaying', 'decentralising' and 'devolving', etc.), the financial logic has played a very important role in the process of the implementation of changes. The British Civil Service has been reduced by one third since 1976 and has significantly improved its resource management, as more power was given to line managers (Clarke & Newman 1997).

The aim of FMI was to improve management of the Civil Service by ensuring that all managers knew what their objectives were and how their achievements would be assessed, had well-defined responsibilities for making the best use of their resources and the necessary information, training and advice to exercise their responsibilities effectively. This was primarily done through the delegation of budget expenditure decision-making to managers, but also accompanied by careful measurement of the output whenever

possible, and the observance of the principle of cost-effectiveness. All the reforms resulted in making Civil Servants more responsible and accountable for their work. Each department works within a limit for its total running costs. This was followed by the Next Steps initiative that emphasised the need to look critically at the functions of the Government and the ways in which government functions are discharged. Decentralisation meant that a central government department would be more responsible for strategic planning, while the day-to-day control was to be carried out by lower level units. This also assumed that all non-pure (non-core) government functions should be discharged by executive agencies, headed by a chief executive, usually coming from outside the civil service. The managers were encouraged to use their full managerial freedom and there were incentives in place to inspire such behaviour. The introduction of strategic planning (although this term was not used explicitly in the related documents) assumed that the agencies and departments were expected to set goals, aims and objectives of their expected output and outcomes, with more or less explicit performance indicators.

In financial terms, FMI had three main elements: 1) delegated budgets, giving individuals at lower levels of management control of resources to match their responsibilities, 2) better information systems that assumed that people on lower levels would know what they do and how they are doing (demonstrated through the costs incurred), and 3) setting clear objectives and performance indicators for individual civil servants. FMI led to the accelerated implementation of advanced, computer based accounting systems and related efficiencies. The objectives-based management initiatives, together with the delegated budgets, raised some fundamental questions about the

management culture of the Civil Service, *per se*.

Overall, the UK experience has proved that managers in the Civil Service performed better when they had a clear view of their objectives, measurable outputs or performance in relation to those objectives and a well-defined responsibility for making the best use of resources, including delivery of outputs and 'value for money'. 'Inputs' are perceived as resources (salaries, accommodation, equipment, etc.), while 'outputs' are the goods and services 'produced' by a particular government unit (department), such as the provision of policy advice, the administration (enforcement) or regulation etc. Finally, outcomes are the effects on the community of an output or a set of outputs. FMI has usually been associated with the first phase of public sector reform, implemented under the Conservative government, led by Baroness Thatcher, which stemmed from the 1979-1983 drive to linearly reduce the number of public sector employees. During these four years, the total number of civil servants were cut by firstly fourteen and then by a further six per cent (Metcalf & Richards 1990).

*Rayner scrutinies* sought to find more efficient ways to deliver the tasks and one of the main conclusions was that further reductions in staffing were feasible (National Audit Office 1986). However, FMI was a child of the second phase that marked the mid and late 1980s, where the emphasis shifted onto improving financial and general management and increasing efficiency, rather than looking for short-term gains achieved through the down-sizing exercise within government departments. The National Health Service (NHS) came into focus and the government required the introduction of general managers in all health authorities (see Harrison, Marnoch and Pollitt 1992). This sustained the drive for performance



measurement in the public sector (Šević, 2004). Resource based budgeting launched in the UK has been one of the novel attempts to look (again) at the allocation of funds to the best uses and ensuring that the ‘best value’ is achieved. It initially began as resource accounting, but is to be developed as resource budgeting, with underlying principles of accrual accounting being used for the entire budgeting process, not only for preparing financial statements and financial reporting (Šević 2004).

Beside the US and the UK, Canada also experimented with PPBS. The system was adopted in the late 1960s, a little later than when it was implemented in the US by President Johnson’s administration in 1965. Canadian coquetting with performance budgeting of an American-style happened before the support for PPBS faded away in the US and led to the discontinuation of the practice in the mid-1970s (Savoie 1994). The fact that the model was implemented when ‘output budgeting’ was in fashion, made sure the Canadian ‘programme budgeting’ model was very comprehensive (Heclo & Wildavsky 1981). In Canada ‘programme budgeting’ led to the design of a fairly comprehensive budget template, based on departmental expenditures in programme budget form. Also, in Canada, the implementation of this model led to the further empowering of the programme evaluation and expansion of the mandate of the supreme auditing body.

The Canadian *Cour des comptes* was able to support actively and eventually, even initiate management reforms that would enable them to perform their duties better and respond more pro-actively to requests by Parliament. This is, to some degree, counter to the practice in Japan, where the Board of Audit has the power to analyse programme performance, focusing on the achieved outcomes, but decides unilaterally to focus exclusively on traditional audit functions –

auditing financial reports of government departments.

### **A Primer of the Continental European Experience: The Case of France**

The French Republic has traditionally been characterised by a *statist* approach to modernisation. To a large extent, this characteristic has been reflected in the *Rationalisation des Choix Budgétaires* (RCB), which was the French version of PPBS, implemented in 1968. The French studied the US PPBS closely in the 1960s, similarly to the British who sent a clerk of the Parliamentary Committee on a fact finding mission. Namely, a group of promising middle level civil servants visited the US in the mid-1960s and were pleased with President Johnson’s Administration experimentation with PPBS (‘output budgeting’). But the design and implementation was also facilitated by the French experience with the National Planning System (Bréaud 1970, Ducros 1976). Consequently, RCB had clear administrative origins as the idea was initiated by civil servants, rather than by outsiders to the public sector, for instance, consultants and/or political advisers (Bréaud & Gergorin 1973); what was going to be, more or less, the case with the NPM initiated reforms, a decade or so later.

Initially RCB had three main functions, those being: (1) to serve as a five-year projection of the national accounts of the country, thus facilitating planning; (2) a programme of major public sector investments and (3) a platform for rapprochement of various stakeholders: government, trade unions and industrialists (employers). Bringing all these interested parties under one umbrella had to facilitate co-ordination between the annual budgetary cycle and the formulation of the National Plan (Green 1980). The shortcomings of one-



year budgetary cycle short-termism were expected to be addressed by adherence to the five-year National Plan (Estrin & Holmes 1983). As with its role model PPBS, RCB was highly centralised (and therefore appealing to the highly centralised French Republic) and co-ordination was entrusted to the steering group headed by the Secretary of State for Budgetary Affairs (Lévy-Lambert & Guillaume 1971). The implementation group had administrative support, provided by the unit especially created in the Ministry of Finance (MoF). This step was undertaken to overcome any eventual resistance from the spending ministries (Hayward 1973). The RCB unit was also closely linked to the National Planning Commission, as RCB assumed close observance of the National Plan. However, the MoF's RCB Unit (often referred to as 'RCB Mission') was never formally subordinated to the Planning Commission (Ashford 1977).

To a large extent, RCB has been a specific 'internal administrative experience' for the French public administration: it was initiated from within, managed from within and guarded from within, as the major opposition was expected to come from within the administration itself. There are claims that the French experience was different compared to other countries that went down the PPBS road, such as the UK and Canada, where management consultants were the catalysts of change who put forward the idea of implementing PPBS. However, it may be true to some extent, but in the British case Parliament (politicians) were genuinely interested in the PPBS implementation and reform of the budgeting process itself. The French RCB was implemented when already there was faded enthusiasm for the PPBS in the US. The French experiment was very comprehensive and inclusive, certainly compared to the UK experience (Heclo & Wildavsky 1981). The main change induced

by the implementation of RCB was the presentation of the draft budget to the National Assembly in the form of departmental programme budgets (Kessler & Tixit 1973). However, the French did not opt to expand the traditional role of the *Cour des comptes*, the supreme audit body. The independence of the *Cour des comptes* has been retained, as the traditional separation of state powers in France was not compromised.

However, the RCB has not delivered as expected (Chevallier and Loschak 1982). RCB failed to gain the trust of departmental heads, mainly because of its high level of centralism. Middle level managers saw RCB as an attempt to reinforce the power of a few senior civil servants (Ashford 1982). Finally, in 1983 the RCB was abandoned (Perret 1994). It is perceived that the failure of RCB influenced the French government not to introduce highly centralised reforms in the 1970s and early 1980s (Fortin 1988). The failure of RCB created a 'collateral victim' such that the credibility of the national planning system has suffered, as the RCB experiment was closely related to the national planning process (Hall 1986). To a large extent, the failure of RCB has also marked the end (or speedy downfall) of the highly centralised model of administration and *dirigiste* ideology, which was especially powerful amongst the *De Gaullists*. Also, the focus on reforming the government in France has shifted from effectiveness, to making the civil service more people-oriented (Clark 1984).

### **Performance Based Budgeting, PPB, PPBS: *Pro et Contra***

Despite the failure of PPB in highly industrialised countries in the 1970s, the very idea to link performance and outcomes to the budgeting items did not make sense. In other (industrialised) countries there have been many attempts to link budgetary spending to

the results of policy actions. For instance, there have been attempts by Dutch local governments to report on expenditures and link those with the outputs initiated by the items spent. In the mid-1990s, a survey of local government entities in the Australian state of Victoria conducted disclosed that 18 out of 122 surveyed municipalities, or 14.8 per cent, used PPBS as their sole method of budget preparation (Bellamy & Kluvers 1995). However, we may not be able to claim that NPM reforms have revived programme budgeting, but they have certainly centred much of the focus on results and managing outputs and outcomes.

All performance based budgeting attempts have been made to move away from the traditional budgeting practices, which focus exclusively on the monetary inputs, rather than what is achieved with the money committed. Traditional budgets are prepared on a line item basis, with only the increments over a previously established base. They tend to allocate resources by increasing the previous budgets by a fixed percentage across the board with changes at the margins. The base is not subjected to any scrutiny and is accepted at face value. Line items are quite often established as a result of political bargaining and reflect the political prestige and power of the respective minister and also his/her ability to handle the Cabinet and Planning Ministry. Traditional budgeting does not provide a basis for 'rational' decision-making and it is difficult to enter the evaluation of results and see whether there is a need for an additional investment in particular uses.

All performance based budgeting models and techniques are concerned with the needs of decision-makers. This issue emerges (or historically has emerged) when there is a strain on the public purse and public decision-makers are faced with the same dilemma as private economic agents – limited funds to be

allocated to a number of growing uses. The public decision-maker is interested in ensuring that the shrinking public purse is committed to the best possible uses, ensuring the best value-for-money. Theoretically, performance budgeting models enable decision-makers to behave in a more rational manner. They have to begin by determining the objectives of the organisation as precisely as possible. Different programmes have to be evaluated and to see what has to be done to achieve the defined objectives. A problem arises with defining the indicators of the impact of the programmes on the target population (social group, etc.). Costs of (alternative) programmes have to be calculated, so that the budgetary allocations can be made against a background of the known (experience-based) cost-benefit relationship.

PPBS requires making a distinction between programme structure and programme analysis. The programme structure offers a framework for matching resources and activities to objectives. In contrast, the programme analysis focuses on the analysis of the costs and benefits of each programme, in other words, for choices to be made. The system requires a higher level of collaboration and co-ordination within the organisation, where different areas have to provide input into the decision-making process. Different departments may have differing, or even mutually exclusive interests, but the PPBS must ensure that all opinions are heard and the best decision (taking into consideration the declared objectives of the organisation) has been made in a timely fashion. The main purpose of the programme structure is to ensure that all the allocations to the same or similar programmes are grouped together, regardless of which department will incur them.

In a traditional budgeting system, cross-departmental spending will be almost

impossible, as each department will have an item in relation to its remit and it would not be recognised that the different items can, in fact, contribute to the delivery of a particular objective. However, the programme structure is rather static and will assist in building a 'matrix', whilst the programme analysis has to ensure that decision-makers are left with a set of options, from which to choose the best one (taking into consideration value-for-money, or whatever equivalent). Programme analysis matches costs and benefits and, taking into consideration the declared objectives, provides information on the theoretically best choice.

As we have pointed out, PPBS require a highly centralised approach and fairly dominant centre, with strong strategic leadership (although the term was not in use in the public sector when the concept was conceived in the early and mid-1960s), which will clearly set out the objectives of the organisation (and its mission, to use the current strategy language). Objectives have to be reflected into programmes, while the programmes have to be broken into programme categories and the latter into programme elements. At the end, the programme elements have to be costed appropriately and the costs have to be associated with each of the programme elements. Cost classification is rather classical, focusing on the nature of costs (salaries, materials, etc.).

Performance based budgeting systems are generally perceived as underperforming in developing countries (Caiden and Wildavsky 1974), but despite this fact, a number of countries, especially in Africa, are attempting to introduce some kind of non-traditional budgeting systems (Malawi, Ethiopia, etc.). Experience has shown that Caiden and Wildavsky may have been right, primarily due to the fact that little attention has been paid to the issue of capacity building and

excessive focus on technical details of budgeting that the countries with a chronic lack of resources and skilled personnel were unable to implement once the foreign advisers left the country. The abstract nature and the lack of operational framework (as pointed out by Wildavsky 1975) are even more noticeable in developing countries, due to the lack of a stable institutional framework. Developing countries do not have the complete data sets necessary for sophisticated planning and programming, beyond the classical percentage *incrementalism*. In developing countries, politics and political process is often more personalised than ideological (Grindle 1980). However, Caiden and Wildavsky (1974) are more against the planning stage, rather than against budgeting in poor countries. In fact they argue that budgeting is more effective because it is more short-term and easier to change and enforce (in an almost permanently changing environment).

However, one should be aware that even mere short-term planning can, in fact, be problematic, due to inaccurate information and the lack of professional staff. There were reports on the chronic lack of professionally trained and competent accountants, especially in Africa (Ronan & Amenkhiennan 1999, Healey & Tordoff 1995). Capacity building in developing countries, in fact, may result in better results achieved in modern planning and budgeting techniques applied. With increased professional competence, the final destiny of PPBS in developing countries may look somewhat different and finally, it may prove that Caiden and Wildavsky (1974) may have been wrong.

## **Conclusion**

As we have seen, Schultze (1968) has listed all the main features of PPBS, which can be considered to be the advantages of its implementation. The practice, even in

developed countries, has shown that the required input information is not readily available. In fact, even if something is definable, it is often rarely measurable. Hofstede (1981) claims that in those circumstances, attempting to implement PPBS would, in fact, represent an error in the choice of management control models. He points out that the appropriate control model, where objectives are ambiguous and output non-measurable, is effectively a political control which may cancel out all attempts to 'rationalise' the budgeting process. Often, PPBS and similar models may prove to be conceptually sound, but in practice irrelevant, as it is difficult to implement them, since all the prerequisites cannot be provided. Although it is difficult to explain why a theoretically sound concept failed to deliver, in the mid-1970s, Wildavsky put forward a bold claim that "PPBS has failed everywhere and at all times" (Wildavsky 1974:205). However, this does not mean that other output oriented budgeting models may fail.

The entire development of strategic management accounting as a discipline has focused on accounting that will enable the organisation to meet its goals, aims and objectives. The recent financial reforms in the public sector have begun with reforms of financial reporting and accounting routines, and culminated with the changes in the budgeting process. The evolution of "recourse accounting" into "resource budgeting" in the UK may be a new attempt at a search for performance oriented budgeting. The drive for *depoliticisation* may again bring other orthodox-rational models of financial management and budgeting in the public sector, especially when the field of policy advice is becoming increasingly politicised. A balance will have to be struck and performance-based budgeting techniques might very well, in fact, fit in.

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## Performance Indicators

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### **Introduction**

Most of the latter part of the 20<sup>th</sup> century was spent in search of an effective, efficient and economical government. It is still difficult to assess to what extent the search was successful, but what is certain is that governments have been growing in size and complexity, which has led to a significant increase in the cost of government. Governments in the Western democracies were exposed to a number of reform attempts since the 1960s, which were supposed to make them more accountable, more effective, more efficient, more economical and more democratic. These trends were intertwined with the constant problem of ensuring accountability of the government and national public administration before the electorate. Most innovations were linked closely with changes in financial planning and reporting practices, but were usually exposed to the destiny of political cycles. Often new administrations have not continued with 'innovations' initiated by outgoing governments.

Performance indicators (PIs) have been connected only with the public sector. Classical financial performance measures that have been employed in the private sector could not be used in the public sector, as profitability cannot be an indicator of the success of public organisations. Public organisations deliver products and services that are often classified as public goods, and therefore excludability cannot be exercised. Even if public organisations deliver quasi-public goods, they must deliver them on behalf of society and profitability is not one of the success factors. Profitability as a success factor also requires organisations to behave in a short-term manner, which again is

not suitable for public organisations which have to take a longer view in order to serve society (the public) better.

PIs require public organisations to take a longer view and relate their current performance with the targets set by other stakeholders and the quality of service offered to the public. The classical business performance model is largely shareholder centred and increasing shareholder wealth has traditionally been the major preoccupation of business enterprises. Even the recent move towards the stakeholder model and balanced business performance measurement in the private sector cannot remove all the legacies of the shareholder bias, as the share analysts still react most sensitively to the financial performance announcements of their target companies. The creation of the Balanced Scorecard (BSC) model marked a more balanced approach to performance measurement, taking into account different aspects of a firm's performance, besides the financial dimension. Most recently, the BSC model has been also advocated for the public sector, assuming that the strategic aspects of public sector organisations can be depicted in a model that will take into account, not only current results, but also embrace developmental aspects. However, whatever model of performance measurement (or management) is used in the public sector, the issue of inputs is raised. PIs are possible input variables and it is important to be able to define them and ensure comparability in order to compare target and achieved results. Nevertheless, it is not easy to define the comparable inputs that allow easy comparability. This is why pre-defining performance indicators is important. Finally, one obtains what one measures for.

### **Definition**

A general definition of PIs can be relatively easily given, but often, the detailed definition

is nationally coloured, taking into consideration different aspects of current national government policies. PIs are a quantifiable measurement, defined in advance, that reflect the critical success factors of an organisation. They generally assist in illustrating how well the organisation is doing in achieving its desired outcomes and meeting the previously agreed objectives. They can also be seen as statements of performance expectations or requirements, necessary for achieving critical results of the position. Often PI is perceived as a numerical measure of the degree to which the objective has been achieved. These numerical measures should be feasible to collect, so that a decision on their success can be established.

As we have seen, PIs are the measure of specific elements of broad construct. They are defined to depict to what extent a particular variable meets the set targets and should also enable an analysis in the cases where the targets have not been, to explain why the particular results have been below the desired level. In practice, organisations focus on the ‘key performance indicators’ (KPIs) which should depict the most important indicators that relate to the key organisational goals and aims. The application of KPIs should enable the design of the evaluation model and should assist in planning the allocation of resources to conduct the evaluation study and ensure that the results of the evaluation process are useful for the organisational improvements.

### **New Public Management Context of Performance Measurement**

PIs are the result of a strong focus on performance measurement in the public sector, perceived as an important part of the wider public management reform. Trends initiated in the 1980s focused on the almost compulsive reduction of costs of modern government, focusing on efficiency, effectiveness and rationality. The New Public

Management (NPM) is heavily concerned with the constant decrease in costs of a “product” and obtaining “the best value for money”. The underlying feature of the NPM model is room for the implementation of a performance measurement/management system. All seven mentioned principles of (new) public management (Hood 1991) are *performance centred* and without performance management, it would have been very difficult to justify the major changes in the public sector. The difficulties of NPM can be focused on from two conflicting perspectives. Namely, performance measurement systems can be a logical consequence of NPM being implemented or, in fact, NPM can be a result of an ‘obsession’ with performance measurement. It may also be possible that both interpretations work.

In a highly hierarchical organisation, there is resistance to change. The formal introduction of a new model is necessary to ignite a change. In our view, this is the case with the continental European models of civil service, where the extent of the public sector is wide and the hierarchy is predominant. Introducing performance measurement/management initiatives usually does, in any case, stimulate further changes. A perception of NPM is given by the OECD which states that “a greater focus on results and increased value for money, devolution of authority and enhanced flexibility, strengthened accountability and control, a client and service orientation, strengthened capacity for developing strategy and policy, introduction of competition and other market elements, and changed relationships with other levels of government” (OECD 1995:37) are the main features of the NPM model. Within this framework, citizens and politicians serve a function of “customers” of the government in the public policy process and are the major players in evaluating the performance of public bodies (primarily



agencies), on the basis of objective information concerning “value received”. Based on that assessment, resources will be deployed or withheld accordingly (*Cf.* Myers & Lacey 1996). It was expected that under the new framework, bureaucratic cultures would be replaced by more entrepreneurial cultures and consequently, the public would appreciate the government more. The public, as a stakeholder, will be firmer in its support of the government and public policy processes will not only be cheaper, but also more effective.

The presence of business-like behaviour called for the establishment of ‘quasi-markets’ as an important, if not key, instrument in implementing NPM-based reforms. A ‘quasi-market’ can be established for the entire country, or on a segment-by-segment basis. It seems that allocation of resources, based on a segmentation approach can give (and has given) generally better results. This had to be reflected in reporting practices as well. The private sector has applied accrual accounting, whilst the public sector resorted to cash accounting, mainly justifying that the government budget is largely cash dependent, being revenue driven (or in simple terms, what comes in as cash can only be disbursed). However, NPM originated in developed countries, with traditionally strong and socially respected governments.

The focus on too many targets and multiple goals, aims and objectives can endanger the success of both economic and public sector reforms, but the initial situations in both sectors required serious actions on behalf of the national governments. It was not only necessary to build new institutions and give them economic “content”, but also to prepare them to be competitive both amongst themselves and with organisations from outside the public sector, which might be outsource-contractors. The government,

especially local government, has “to reinvent” (Osborne & Gaebler 1992) itself in a very volatile environment. The reinvention process may start begin with focus on accountability and technically, accountability can be achieved by promoting performance measurement and focus on performance indicators, as it outrightly shows what has been achieved by the monitored organisation.

Transition and developing countries have endorsed the practice of performance management, usually as a part of major public sector reform. To a large extent, the models applied are those of advanced democracies (developed countries) with some or no adjustments. The uncritical application of Western models often creates many problems, as measurement in fact does not make much sense. For instance, measuring the effectiveness and efficiency of the national health system institutions in the country where patients have to purchase necessary medicine and medical materials themselves before being admitted to the hospital, certainly does not make a lot of sense. Similarly, developing a model that is far advanced for a country can have an adverse effect and in fact, initiate counterproductive behaviour that spurs monitored agencies to hit one or two main indicators, without the necessary focus on the whole picture (Šević 2003, Šević 2005).

In fact, it seems that the private sector in transition countries has by far been more successful in the appropriate application of advanced measurement systems and consequently developing PIs that suit the strategic needs far better than in the public sector (Tekavčič & Šink 2002a; Tekavčič & Šink 2002b; Tekavčič & Šink 2003). However, simply by working on the development of a performance measurement system can initiate better performance of (local) government organisations (Šević 2005). There are also examples of good

practices in effective communication with the electorate (citizens) regarding the (local) government performance and targets met (Jakir-Bajo 2003)

### **Developing PIs: Selection and Design Criteria**

In order to develop PIs, a (public) organisation has to have well-developed goals, aims and objectives. PIs and/or KPIs can be defined from within the organisation or simply imposed by outside stakeholders. Whatever the process of definition and implementation is, PIs have to be comprehensive and capable of supplying the information on organisational performance and reflecting the organisation's goals. KPIs must be the key to its success and have to be measurable, or in other words – quantifiable. The definition of PIs and the rules for measurements are to be fixed for a longer period of time, as long as the organisation's goals, aims and objectives are constant.

PIs require meeting a number of criteria: 1) differentiable; 2) observable; 3) consistent; 4) achievable; 5) measurable; 6) clearly stated; 7) relatively exceedable and 8) adequate. They have to ensure that they can differentiate between standard and substandard performance, allowing the observer to clearly make a distinction. PIs are to be observable i.e. that they can be noticed and that they create a change in the environment that clearly creates some kind of consequence. PIs are to be consistent over time. They should not be perceived as static, but also they should not be changed very often, as this will put the organisation in the uneasy position of not knowing in which direction it is moving. PIs have to be set to be within the reach of the organisation, as otherwise they will lose their purpose. PIs that cannot be achieved will demoralise the organisation and its employees and will create adverse effects. Measurability means that PIs

can be compared to a set standard and through comparison, the results can be defined. An organisation's documents have to highlight clearly the PIs and what the expected levels of achievement for the organisation and its sub-units are. They have to be documented, but also can be informally communicated throughout organisations so that employees buy-in and endorse the set targets. Moving the targets further and further has adverse effects, as again the organisation may resort to reactive, instead of pro-active behaviour. Good PIs should be achievable, but also should be set in such a way that allows very successful organisations to overshoot the target. Practice has shown that well defined PIs allow above-average organisations to overshoot them by up to ten per cent. Finally, the PIs have to demonstrate that they are adequate, that is that they are sufficient to depict the organisation's performance and that there is no need to introduce other PIs or KPIs in order to ensure that a set of PIs depicts the real state of the organisational performance.

PIs focus on critical results, which are seen as the key duties and responsibilities associated with a particular unit or sub-unit within an organisation. In a well-designed organisation, each unit should be in a position of knowing what the critical results are and what they have to achieve for a particular level of performance. Normal professional practice is to organise a meeting of key stakeholders and through a brainstorming session, produce a list of all possible indicators that may reflect organisational performance. Usually the lists are fairly long and the indicators often can be contradictory, cancelling one another's effectiveness. It is then necessary to see what the indicators are, that can grasp in the best manner, the major performance variables. Often, the indicators that are organisationally supported are those that can be used in intra-organisational

politics to secure dominance and the upper hand. Similarly, government advisers in their memos, usually reflect upon the practice of using KPIs for intra-government frictions, or even for closing those programmes that may not be performing well.

PIs are to be linked with related categories such as performance standards and performance targets. Performance standards (PSs) are to be seen as the minimum acceptable level of service provision that has to be met by an organisation in the exercise of its particular function, and measured by reference to a PI for that function. Performance targets (PTs) are defined as a level of performance in the exercise of a particular function that an organisation expects to meet in future year(s), as measured by reference to the PI, in relation to that particular function. More recently, sub-national (local) public sector organisations are driven to achieve results defined by best value (for money), especially in the UK. Within that particular (“best value”) framework, there are sets of Best Value PIs, which are defined as a national measure of performance, set by the central government. In setting the best value PIs, the central government usually takes into account the prior results at aggregate national level and general trends of improving effectiveness and productivity. Also, more recently, international benchmarking has become popular, where national governments compare the trends in other jurisdictions and see how their own results relate to them. This has generally been a fairly successful practice in Europe, but was driven more by political factors in favour of tighter European integration, rather than the need to compare the public sectors and their efficiency in different countries.

Local governments in the UK are also required to develop the Best Value Performance Plan (BVPP), which is an

annual report that provides details of current performance levels, actions of the local authorities to address any shortcomings and future performance standards expected to be attained by the local council/authority. Local governments are also expected to produce a Comprehensive Performance Assessment (CPA) which is, in fact, a framework for measuring the overall performance of a local authority and its bodies, using best value PIs, best value inspection reports and externally produced audit reports. It has also been noted that interest in performance audits is increasing, especially in those countries that are prominent champions of NPM reforms (such as Australia). Whilst the UK opted for the use of the term “best value”, the Australian public sector documents refer to the same concept as value-for-money (vfm). These performance audits are to ensure that the best choices have been made, not only in terms of financial prudence, but also in terms of outputs/outcomes per unit of input. It is possible to opt for the cheapest option, which will not deliver the expected outcomes and then an additional input (at additional cost) is required to achieve the promised results. Consequently, the ultimate cost will be higher than initially envisaged. PIs are to be developed in a manner that will allow outside auditors to report on their credibility and accuracy. It is usually perceived that a performance information audit has a twofold focus on financial information and reporting, based on the requirement of best value (value-for-money) reporting (Barzeley 1997).

Well-defined PIs have to reflect clearly upon the organisational values and underlying philosophy. It is also necessary to clearly define clients (stakeholders) and their needs. It is also necessary to have aims and objectives which specifically outline what has to be achieved in relation to the stakeholders’ needs and to identify clearly each and every phase in the process of services delivery, and

what is to be achieved at each particular phase of the process and how it will be achieved. Organisational values and philosophy should be readily available from the organisation's strategic documents, primarily its mission statement and strategic plan. Often, organisations have very broadly outlined goals, aims and objectives and those somehow fail to stress the organisational values in the best possible manner. It is also possible that the mission statements are influenced, more than was expected, by temporary fashions. For instance, many top universities in the world have, as their stated mission, to educate tomorrow's leaders, formulated in one way or another. This is an achievable target for the national top university in any of the countries observed, but there is a problem if a number of universities, especially in a small country, rightly or wrongly believe that they will educate their future leaders. Identifying clients (or more broadly stakeholders, see: Šević 2004) may prove to be a difficult process, despite looking fairly straightforward. Often, clients or customers may play fairly different roles in the process and therefore their position may prove to be complex and blurred. For instance, under the NPM framework, students are universities' customers (clients). However, it is somewhat unclear, *stricto lege*, what their legal status is, as customers. Do they pay for the service with a guaranteed outcome (a degree, and with a better chance of good employment), or simply pay for having access to education? So, a PI that measures student satisfaction can prove to be a double-edge sword. Students may be more satisfied with an underperforming lecturer who will "coach" them for an examination, ensuring that they will have good marks, than with a very good lecturer who focuses more on the process of learning, ensuring that students are exposed to the latest developments in a given field, but

does not "teach" them how to pass the examination successfully. This is why it is necessary to define, almost simultaneously, both the clients and their needs. With the definition of needs, it is necessary to ensure that aims and objectives clearly point out what is to be achieved with respect to those needs. The delivery of a service is a process that usually has several phases. Connecting each of the phases of the services delivery process with a measurable expected output and outcome is necessary, in order to ensure that the performance is measured.

In the process of setting up PIs full co-operation is required between the organisation and the stakeholder, primarily clients/customers. Clients have to acknowledge and articulate their needs. Clients have to have a general idea as to what has to be done to meet their needs and what their general expectations are. Usually, clients' expectations are socially driven and change over time. With the improvement of the delivery process the clients' perception of their needs and expected level of service will evolve. It should also be noted that clients may be supported by a public organisation (local government, etc.) in developing their perception of their own need. Cultivating clients can be very useful, especially in areas that are fairly novel and where clients do not have prior experience with those services or models of service delivery. This, for instance, can be the case with students who can be supplied with the student's charter (or a similar '*service first*' style document), where the University, as a public provider, makes certain promises and assists in cultivating expectations in their customer base. So, the clients are clearly told what they can reasonably expect from the provider and what goes beyond the regular organisation's remit.

PIs may focus on different aspects of the service delivery process, organisational and individual learning and the financial health of

the organisation, etc. Whatever their primary focus might be, they have to be put in a relative strategic congruence, ensuring that they will not be in conflict or endangering the overall usefulness of the performance measurement (performance management) model. As has already been pointed out, there are cases of abuse of PIs, especially for the purposes of short-term political benefit. This is best observed on the eve of any general or local elections, where the PIs used and reported many years ago are taken out of the wider context and used to “prove” the (in)efficiency of a particular political party or a political contender. Therefore, it is necessary to note that PIs are to be used within the system of performance measurement (performance management) and only there, can they really provide information on the relative performance of the organisation and be used to devise the policy actions that can improve the outputs (outcomes) of the service(s) delivery processes.

### **A Possible Typology of PIs**

PIs are usually prepared for a particular service and grouped to grasp the specifics of the delivery process and expected social outcomes (and/or outputs). For instance, possible PIs for local (provincial) social services can be: the number of permits for half-price travel or less on eligible services, issued to elderly persons per 1,000 population of pensionable age; the cost of a concessionary scheme per user, number of designated car parking spaces for people with disabilities, per 100 public car park spaces; percentage of adults arrested and referred to a drug treatment programme who completed their programme; the proportion of repeated offending amongst drug misuse offenders, percentage of visits to collect syringes and needles discarded in public places undertaken within a targeted time, etc. (source: UK Audit

Commission). Each of these indicators can certainly shed some light on the performance of an observed social security service, but these indicators can also be problematic if they are used in an idolatryc manner. Namely, a social service unit operating in an affluent area, with a relatively small number of drug offenders can fall seriously below the national benchmark on some (or even the majority of ) indicators, primarily due to the social stratification of the local population. It may be that the majority of its residents are not in need of receiving social support, but the services have to be offered anyway. So, if the output/outcome is not linked to the unit of input used, the aggregate results will certainly be misleading.

The majority of performance measurement/management models regard PIs in terms of inputs, processes, outputs and outcomes. Inputs are resources required, to be put through the process, which are the way in which the services are delivered. Outputs are activities of the organisation, or the service it provides, whilst the outcomes are the impacts of the services. The focus on outcomes can be manifold, as outcomes can be seen as activities, immediate outputs and social consequences or final outcomes (Levitt & Joyce 1987). The Financial Management Initiative (FMI) launched in the UK in the early 1980s revolved around *economy*, *efficiency*, and *effectiveness*. Later *efficacy* and *electability* were added (Flynn et al. 1988), followed by *equity* (Pollitt 1986). In practice, public sector organisations perceive economy as a pure cost control exercise, either through budgetary control or through minimising resource consumption (see: Jackson & Palmer 1988). Efficiency is understood as being the ratio of inputs to outputs in nominal terms, or as the rate at which inputs are converted into outputs. Effectiveness is a concept that is fraught with ambiguity and confusion. The UK Treasury

perceived effectiveness as the ratio of output to planned output (Pollitt 1986) or how far output achieves government objectives (Jackson & Palmer 1988). The Civil Services may distinguish between administrative and policy effectiveness, where the former looks at the way the services are delivered, whilst policy effectiveness focuses on what extent policy impacts meet policy aims. Equity is the most problematic to define, as it is usually narrowed to administrative justice, that is allowing access to service to all those entitled. It is a basic rule that equity is at the bottom of every PI.

PIs are to address all aspects of the model, but it is usually very difficult to create indicators that will be able to address them simultaneously. PIs are usually clustered as a group, to address one of the aspects of the model. PIs can be *prescriptive*, *descriptive* and *proscriptive*. Prescriptive PIs are those which are linked to the objectives or targets. Descriptive PIs, in contrast, record changes in variables, whilst proscriptive PIs list activities and/or states that should not happen in a well-run organisation. This is the why the latter are also called negative PIs. Often, external forces are in favour of prescriptive PIs, as target setting is a very popular device in controlling an organisation. However, in practice, PIs are far too often used in a descriptive manner. This is partly due to the fact that organisations prefer to have their performance mapped and partly due to the fact that a comparison of past and future performance is often used for assessing organisational success.

### **Challenges of Performance Measurement and PIs**

PIs came into focus with the implementation of NPM reforms in Western developed democracies. Although the reforms were formally promulgated to de-bureaucratise the public sector and bring voters into the centre

of decision-making, they were, in fact, largely driven by financial concerns and attempts to reduce the costs of the public sector. The three 'E' model initiated PIs which failed to grasp the quality of service delivery (Pollitt 1987). Quality issues have also brought customers/clients to the centre of attention. Strategic focused performance measurement systems (such as the Balanced Scorecard – BSC) included, as a perspective, customers/clients, as they are the ultimate users of goods and services offered by the public sector organisations and their feedback should be used for improving the quality and focus of the service.

PIs should enable organisations to embark upon a process of continuous improvement. They can be used for monitoring the overall strategic or organisational performance, as an instrument of control over the lower layers of the organisation, or can be used for assessing the work of employees and determining the level of their pay. This eclecticism influences the process of defining PIs, as often the organisation tries to define PIs in such a way that they can depict changes in a number of observed variables. Different interest groups, both within and outside the organisation, will have diverse interests and they will support different definitions of performance and consequently uphold different measures (depicted by different PIs). It also became clear from practice that politicians prefer PIs that are somewhat ambiguous and can be interpreted in numerous different ways, depending on the political needs. This somewhat conflicts with the objectivity criteria of PIs, but it usually does not concern politicians very much. Often, in practice it may not be clear what purpose PIs are in fact serving and what a good indicator is.

Different political groupings may have different perceptions of good PIs. Those concerned with the financial aspects of service delivery, will certainly support those

PIs that focus on efficiency, while politicians who are at the eve of re-election would rather look at effectiveness and to what extent the electorate is satisfied with the administrative performance of the public sector. Definitions of PIs must be clear and consistent, in order for PIs to be deemed to be good (well-defined). PIs should measure performance that is owned by the organisation and not dependent on external factors or environmental factors, which are not very often easy to comprehend and control. Also, a good PI will be relevant to the needs and objectives of the organisation. Functioning PIs have to be endorsed by the organisation and seen as delivering value to the organisation and its members. Imposed PIs are usually short-term limited, as organisations can find ways to circumvent their focus. Whatever PIs are developed, they should not be perceived as static, but the organisation should be supported to work on the development of new PIs in a systematic way that will not hinder the focus and reason of the existing PIs.

## Conclusion

The public sector, in the second part of the 20<sup>th</sup> century, has been thriving to justify its existence and to deliver services to citizens with increased quality and with constantly falling input levels. Historically, there have been numerous attempts to develop systems for measuring organisational success in the public sector. In the private sector, the organisational success has traditionally been measured as profitability and predominantly in financial terms. Since the 1980s this has been changing in the private sector, but business surveys still disclose that financial variables are predominant in assessing organisational success in the private sector. In contrast, the public sector, due to its very nature, is impossible to measure by financial criteria. Financial variables are traditionally

the input in the public sector processes. In order to capture to what extent the public sector discharges its function, a set of PIs is developed, trying to capture the most important variables in the public sector service delivery processes. Growth of PIs and performance measurement fashions have been recorded since the early 1980s, with a growing interest in ‘reinventing government’ (Osborne & Gaebler 1992).

PIs are initially to be developed by public sector organisations, taking into account strategies that they have adopted. However, practice has shown that PIs are often defined and imposed by government, as the main (and usually the only) contractor of public sector services. The more recent concepts of “best value” and “value-for-money” require public organisations to compare and compete, promoting rankings and excellence lists. However, most PIs fail to pick up developmental components and do not capture well the qualities of quickly developing organisations. But, despite all the shortcomings that we have presented, PIs and their use in the public sector has been in constant growth and it is most unlikely that this will change in the near future. The culture of performance measurement and/or performance management is here to stay, despite all the shortcomings that have constantly emerged, requiring serious management attention.

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## Policy Elites

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### **Introduction**

The modern approach to elites in democratic societies has its roots in the political and sociological works of Gaetano Mosca and Vilfredo Pareto, whose observations on elites emerged in reaction to three major trends at the end of the nineteenth century: the Marxian conception of historic materialism; the simplistic association of the actions of representative government with the will of the people; and socialist political rhetoric on serving the needs of the working class. Mosca and Pareto also influenced Robert Michels, who contributed the influential ‘iron law of oligarchy’ to elite theory.

These three scholars wrote the classics of elite theory to strip the romanticism from interpretations of political and policy process associated with all forms of government. In this broad sense, their critical work is consistent with the general European intellectual tradition. However, their important writings had only a delayed impact on the emergence of elite studies in the English speaking world. The classic American approach was probably most associated with C. Wright Mills, who, although aware of the contributions of Mosca, Pareto and Michels to elite theory, was more directly influenced by Max Weber. Mills assigned a significant role to the interdependence between elites from bureaucratic institutions that undertake diverse social functions, and of circulation of elites between these institutions. His approach to elites triggered a reaction from scholars who advocated an alternative explanation. Most notably, Robert Dahl, a political scientist, used the notion of ‘pluralism’ to defend democratic arrangements from the claim that elites manipulate and dominate the

political and policy process. Both elite theorists and pluralist political scientist were criticized by scholars who utilized the Marxian critique of capitalism to consider the role of economic and political elites in relation to the social relations of production under capitalism.

In much of what followed, there was a focus on economic elites and on political elites and their ‘networks’. Also, there has been greater interest in the general relationship between elites and policy processes, particularly the influence of private ‘think tanks’ on policy development.

Since the 1980s, there has been popular reactions against social policies perceived to have been devised by elites. This suggests that not only has there been some dissemination of the ideas of elite theorists across the broader community, but that the public do not automatically embrace ideas associated with the ruling class. In short, popular sentiment can act to constrain the effectiveness of policy elites. As such, understanding of the relationship between elites, the masses and policy is not just important for social theory, it is also important for issues of governance, such as the appropriate level of political, and fiscal, decentralization in society.

### **Elite Theory – The European Classics**

In *Die Deutsche Ideologie* (1845), Marx and Engels stressed that class relations are a social product and that the ruling class dominates economic forces and social ideas. “The ideas of the ruling class are in every epoch the ruling ideas ... The ruling ideas are nothing more than the ideal expression of the dominant material relationships, the dominant material relationships grasped as ideas; hence of the relationships which make the one class the ruling one” (Marx & Engels 1845:67). Social history, in the Marxian sense, came to be considered as ‘historic materialism’

because Marx's study of history suggests that control of production also came to be associated with the control of ideas and ideology, with the ruling class providing ideological support for the class who control production.

To a considerable extent, the emergence of elite theory in Europe was intended to modify and qualify the Marxian conception of the ruling class in historic materialism. In addition, it was intended to expose the naive and simplistic notions often raised in support of democratic 'representation' and 'socialist' policies. The term 'elite' derives from the work of Pareto. However, the first substantive contribution to this field is now usually credited to Gaetano Mosca for his influential *Elementi di Scienza Politica* (1896), with less developed aspects of the elite approach also evident in Mosca's earlier works such as *Teorica dei Governi e Governo Parlamentare* (1884).

Mosca's goal was to highlight the role of a ruling stratum, which he labeled the 'ruling class'. The ruling class is essentially the organized minority that forms the hierarchy of officials from coordinating political bodies. The key element of the relationship is that the ruling class justifies their power by appealing to the sentiments and beliefs of the other classes. He called this the 'political formula', whereby the policy program devised by the ruling class is presented to society as the popular will, or a range of other similar phrases. Importantly, the relationship between the ruling class and the rest of society was not presented as unidirectional, and the role of social equilibrium was given some consideration. However, the ruling class was treated mainly as a higher stratum of the political classes, with limited indication that the ruling class may include elements from outside politics. Furthermore, the sociological foundations of the relationship

between the ruling class and the rest of society were not significantly investigated.

Nevertheless, Mosca accepted that the power of the ruling class to persuade and influence the masses in society is significantly constrained by sentiments prevailing across the community in a particular time and place. If those sentiments are consistent with the policies being advocated by the ruling class, or the ruling class can associate its policies with the prevailing social sentiments, the social equilibrium is likely to be maintained and elite domination of policy will be successful. However, when policies are inconsistent with the prevailing social sentiments, the social equilibrium may not be stable and ruling class policies are less likely to be adopted. Consequently, the ability to rule is not just dependant on the ruling class, but on the capacity of the ruling class to demonstrate that its policy program is consistent with sentiments associated with the will of the people.

As a consequence, Mosca did not accept the deterministic link between material interests and ideology suggested in early Marxian studies of historic materialism. Instead, he interpreted the ruling class in a system of representative government as a mixture of elements, some with an 'aristocratic tendency' and others with a 'democratic tendency'. The elements demonstrating an 'aristocratic tendency' act to maintain and defend the old ruling class arrangements, while the elements demonstrating an 'democratic tendency' act as agents of rapid change, with the old ruling class being replaced by the new ruling class. According to Mosca (1962:390), the best political regimes has a good mix of aristocratic elements, to defend and ensure the survival of political arrangements under a given social equilibrium, and liberal-democratic elements to provide renewal in the

ruling class and prevent political actors from becoming stale.

Pareto's main contributions to elite theory concern his explorations into the relationship between political and economic classes and the provision of a theoretical framework that account for a broad range of sociological influences on elites and policy. While his ideas evolved over time, his critical appreciation of Italian politics remained a constant motivating factor in his contribution to elite theory. In the early 1890s, Pareto (1893) had concluded that political parties in Italy exist in name only and that socialism had emerged to an extent that private incentive was almost nullified. In particular, he regarded Italian politics as a mechanism through which the upper classes enrich themselves, with the bourgeois of northern Italy supporting elements of 'industrial socialism', either along the lines being advocated by socialist leaders like Filippo Turati or by advocating special industrial arrangements with government, and with the bourgeois of southern Italy advocating agrarian socialism. The net political effect was the nationalistic and dogmatic styles of government associated with the Italian Prime Ministers of the day, Giovanni Giolitti and Francesco Crispi. In this context, Pareto interpreted policy struggles as centering around the relative balance of agricultural and industrial protection and corresponding issues such as the relative importance of trade and other relations with Germany and Austria on the one hand and France on the other. His major concern with this environment was that the character of government becomes interventionist and militaristic, resulting in imperial expansion, rapid growth in public spending, increased rates of issuing of currency, public debt and public banking crisis (which occurred in the early 1890s). Importantly, these were major concerns because Pareto regarded the general burden of

such arrangements as falling heavily on working classes. His initial motivation in discussing these issues appeared to be a desire for change: to reveal the material interest of elites in the political process and the material cost to the lower classes. However, as time progressed and his hope for influencing political arrangement diminished, Pareto's motivation was modified to that of a simple desire to deal with 'social facts' of government in Europe and to develop general social theory.

In his first major book, *Cour d'Économie Politique* (1896/97), Pareto investigated the general principles of social organization in terms of Herbert Spencer's sociology and social evolution. He introduced the notion of aristocracy, or the 'best', when noting the heterogeneous character of society, and in stressing how the aristocratic classes gain and lose power. The issue was developed significantly further in "Un'Applicazione di Teorie Sociologiche" (1990), in which Pareto contended that the majority of human action is primarily motivated by a mix of sentiment and logic, not just logic. The fundamental theoretical feature of this study, which came to be the foundation stone of Pareto's system of social equilibrium, is that the real phenomenon acts to modify the subjective phenomenon and *vice-versa*. That is, there is an element of dual causality whereby policy outcomes alter preferences and preferences shape policy outcomes. Importantly, this applies to 'aristocracies' as well as the broad civil population, although not in equal measure: the sentiments of the aristocracy are a less volatile force on the conduct of the aristocracy than it is on individuals who, in aggregate, comprise the masses.

Pareto used the interaction between the real (policy outcome) and subjective phenomena (preferences) to analyze and explain what he referred to as three 'facts': the period or duration of social crises; the

collapse of the aristocracy; and the rise of a new aristocracy. The first fact was explained in terms of a growing intensification of 'sentiment', such as socialism, nationalism, humanism, imperialisms, jingoism or a range of other *isms*, motivated by opposition to the prevailing aristocracy. The second fact is, according to Pareto, either due to the aristocracy's lack of willingness to defend its power; or its rights being usurped by others, with benefits appropriated for the good of members of competing aristocracies. The third fact closes the circle. The rising aristocracy feeds the illusion by perpetuating the belief that it stands with the people in opposition to the aristocracy that is in terminal decline. The sentiment that inspired the civil population may well be used by the new aristocracy, becoming more rigid and closed to public ideas once it has gained power.

In his *Les Systèmes Socialistes* (1902-03), Pareto introduced the term 'elites' to his analysis. From that moment on, the field became almost unanimously known as elite theory. In this work he integrated his earlier discussion of elites with the general question of social selection and distribution. This is important because it makes the direct link between elites and wealth, and the difficulty (but not impossibility) of altering the general pattern of the distribution of wealth irrespective of which elite group governs. Pareto's purpose here was to highlight the major obstacles that socialist regimes would face if they attempted to alter the distribution of wealth. He viewed their arguments on this matter as illusory, and just the latest historical example of a period of crises where a potentially new elite was battling for the hearts and minds of the civil population in an attempt to replace the prevailing elite. However, he was not adopting a purely anti-socialist stand, as the same argument was applied to liberals, democrats or a range of

other groups. Social and political oscillations are a general phenomenon, and linked to the rise and fall of elites, regardless of the beliefs and sentiments advocated by the new potential elite.

Pareto was to significantly extend his sociological analysis of elites and masses in the *Trattato di Sociologia Generale* (1916), regarded by many as Pareto's greatest work. However, before this work was published, Robert Michels published *Zur Soziologie des Parteiwesens in der Modernen Demokratie* (1911), in which the iron law of oligarchy was introduced. Michels placed more emphasis on the organisational features of institutions than Pareto, who was more intent on pursuing general regularities not tied to any particular social form. Michels contended that, across the masses, there was a psychological need for leadership and that the conditions by which organisation provide such leadership is essentially cultural. Hierarchy and bureaucracy are common across all forms of social institutions.

The key difference between general hierarchy and the ruling class in the political order is that representative government has access to public funds, through the fiscal system. Persuasion is seen as possible through a close relationship with the media, and the 'State' has access to more direct forces, such as the police and the armed forces. Like Mosca and Pareto, Michels considered ruling classes, or elites, a general phenomenon of social organisation, which is applicable to political arrangements in all forms of government.

In developing his iron law of oligarchy, he played the devil's advocate. That is, he identified the social tendencies that are necessary to defend the will of the people under democratic arrangement from the encroaching influence of the ruling class. He found that extensive use of referendum was unworkable due to the associated time delays.

There could even be social paralysis as issues wait to be resolved. Political and other leaders would need to renounce their benefits from being associated with the elites, but at best, such events are ad hoc, partial, and symbolic. Attempts to replace the ruling classes with syndicates from the masses would be likely to result in union autarchy. Finally, anarchism could take hold, but history suggests that anarchism is more of a 'faith' than a practical option.

Michels was pro-democratic in the sense that he regarded the progression of political organisation closer to the democratic idea as meritorious. His work on elites is therefore usually considered as an example of democratic elitism, as are aspects of the work of Max Weber and Joseph Schumpeter (Ruostetsaari 2003). Nevertheless, Michels regarded democracy more as an ideal to pursue, than an attainable goal, suggesting that oligarchy was an iron law in sociology across all social forms.

James Meisel has succinctly captured the core of the classical elite system of Mosca, Pareto and Michels by referring to the three C's of group conduct: "consciousness, coherence and conspiracy" (Meisel 1962:4). The impact of these studies on the English speaking world is noteworthy. While the early work of Mosca and Pareto on elites predates that of Michels, it was Michels' work that was first disseminated among the English speaking community. His seminal work was translated as *Political Parties* and first published in English in 1915. Mosca's *Elementi di Scienza Politica* was translated as *The Ruling Class* and only published in English in 1939. Even more puzzling, Pareto's *Les Systèmes Socialistes* has not yet been translated into English, and his essays on elites were only published in English in 1950 under the title *The Ruling Class in Italy before 1900*. Nevertheless, the intellectual legacy of elite theory is most strongly

associated with Pareto, even in English speaking countries. This is because Pareto's 1916 *Trattato di Sociologia Generale* provided the definitive classic study in the tradition of elite theory.

The Paretian theory of social equilibrium emerged in his *Sociologia*, and is important because it incorporates a considerably enhanced role for elites in the theoretical representation of the social system. When it was translated into English and published in 1935 as *Mind and Society*, the four volume book received with a mixture of high praise and utter contempt. This 'notoriety' no doubt contributed to Pareto's legacy as the primary classical elite theorist. More importantly, his magnum opus was taken seriously at leading international Universities. For example, a Pareto circle developed at Harvard University, with many of the thinkers who participated in this circle becoming leading twentieth century social theorists.

Social equilibrium is the term that Pareto gave to the social state. The key issue is whether this equilibrium is stable or unstable. However, social equilibrium was used by Pareto as a generic term to describe three related factors: the economic state, the political state and the social-behavioural state. Equilibrium in the economic state is determined from a combination of economic theory (static market outcomes) and elite theory (economic dynamics). The prevailing economic balance is interpreted as a struggle between economic elites, with the outcome depending on the relative access to capital by risk taking 'speculators' and risk averse 'rentiers'. Equilibrium in the political state concerns the balance of power between elite groups - between astute and cunning 'foxes' and forceful and direct 'lions'. This is expressed as a political balance between the rights of the individual and the rights of the state, with the elites employing strategies that mix persuasion and force in an attempt to

secure political authority. Persuasion is an indirect technique based on quasi logical rationalizations, what today would be termed 'spin' but what Pareto called derivations (because the rationalizations derive from sentiment). Equilibrium in the social-behavioural state concerns the distribution of sentiments across society. Pareto used the term "residues" for sentiments, but his focus is on whether popular sentiment is conformist (acting to preserve the prevailing social-behavioural state) or non-conformist (acting as a force for change).

A stable social equilibrium requires stability in the economic, political and socio-behavioral balances. Elites play a crucial role in the first two balances. However, the socio-behavioural balance is largely set by the psychological profile of the members of society. As such, this acts as a generally constant constraint on economic and political elites' capacity to influence the masses, either by force or persuasion. Instability in any of the economic, political or socio-behavioral equilibria will interact with the others, causing social equilibrium to become unstable. Crisis, and the fall and rise of elites, is an outcome of instability in the social equilibrium. Stability of the social equilibrium is associated with the continuing dominance of the political elite and/or the existence of a non-violent and generally agreed mechanism for changing the governing elite without plunging society into crisis. Pareto applied his general sociology to contemporary society, mainly in Italian society, in his 1921 book the *Trasformazione della Democrazia*.

### **Elitism vs Pluralism**

The importance of classic European studies in elite theory became more widespread in the English speaking world from the 1940s. Particularly significant in this regard was James Burnham's *The Machiavellians*:

*Defenders of Freedom* (1943), which played an important role in disseminating the ideas of elite theorists. In particular, he traced the influence of Machiavelli's methodological approach, which demanded scrupulous consideration of "what is" in a manner that is devoid of sentimental illusion, upon Mosca, Michels, Pareto and others. Also, in the *Comparative Study of Elites*, Harold Lasswell, Daniel Lerner and C. Easton Rothwell (1952) proved influential in applying elite theory. The practical relevance of elite theory was not lost on public administrators. Of most note is the 1954 manual prepared for the US State Department by Alfred De Grazia, in collaboration with Paul Deutschmann and Floyd Hunter, titled: *Discovering National Elites*, and subtitled: *A Manual of Methods for Discovering the Leadership of a Society and its Vulnerability to Propaganda*. This remarkable document outlines methods, such as sampling and content analysis, for analysing formal elites (such as political parties, bureaucracies, religious groups, business organisations, trade unions, the military and the media); informal elites (which may include elements of the intelligencia); and the interlocking relationships between formal and informal groups. Particular attention is given to identifying the leadership of elite institutions, the plurality of elite structures, and mapping the mobility of elites to consider power shifts. The manual presents this information in the context of gathering intelligence and in determining the vulnerability of elite leaders and groups to 'communications'.

In addition to practical use of elite theory, the next great episode in the development of elite theory also emerged in the United States. In the case of the European classics there was general agreement on matters of substance, although there was considerable dispute on the 'priority' for original ideas with accusations of plagiarism directed against

Pareto for not acknowledging Mosca's work (as discussed in Meisel 1965). In contrast, the American treatment of elites in society in the 1950s was heavily contested at the substantive theoretical level. Specifically, competing views were advanced by advocates of: the power elite approach, as initially developed by C. Wright Mills, the pluralistic philosophy of democracy developed by Robert Dahl; and the critical sociology of radicals working within the Marxian tradition.

Mills' classic 1956 study on the *Power Elite* provided a dualistic contrast between mass society and the power elite, where development has resulted in a concentration of power that is both dense and interlocking. Moreover, such concentration of power resulted in a greater incidence of impersonal immorality. That is, the relationship between institutions that facilitated the concentration of authority in the hands of the power elite provided the impersonal basis of relations that took immorality to new highs (or lows). Mills' thesis was provocative. Gone was the attempt at value neutrality advocated in classical elite theory when focusing on 'general' phenomena such as social oscillation and the associated rise and fall of elites. While the classics recognized the importance of social sentiment as the cement that holds society together, and the clash of sentiment that causes it to crumble, they adopted an almost post-modernist reluctance to ethically assess societies at a point in time, or a society at different points in time under the direction of different elites. In contrast, Mill dealt with a specific form of society, mid-twentieth century United States, and not in a value neutral manner, but in a manner that includes value judgments which associated concentration of power with moral decline.

The central feature of the power elite is that the economic, military and political structures have become progressively more

interlocked, and the institutions associated with these structures, namely corporations, the army and government, have become enlarged and centralized. At the 'pinnacle' of these institutions, 'higher circles' have established. These comprise the economic, political and military elites, which in aggregate comprise the 'power elite'. The direction of influence in this system is largely unidirectional: corporations, armies and governments shape modern life, with all else either being subservient to the power elite or else a means to their ends.

Related to this characterization of the power elite is the notion of professional 'celebrity'. Each of the big three institutions have celebrities, or individuals who are the focal point of entertainment and public information. They are the creation of the elite, and as such serve the interest of the power elite. However, the ruling class is not presented by Mills as omnipotent. It is comprised of individuals, some of who are conscious of their social class, others are not. The strength lies in their interconnectivity: in the links between money power and celebrity. As such, this represents a repudiation of the evolutionist basis of classic elite theory which characterizes members of the elite as the best, with the most energy and the greatest desire to be influential. In short, the classical association of the elite with the best, subject to some imperfect social selection, is replaced a concern with the interconnections between the elites of the centralized economic, military and political organizations.

The reaction to Mills' thesis was forceful. Perhaps the most important reaction was Robert Dahl's (1958) "A Critique of the Ruling Elite Model". Dahl first excludes from his definition of elites any controlling groups that are an artifact of democratic rules, such as where the 'real' rules of political selection permit the majority to dominate if the individuals that comprise the majority choose



to act in a manner permitted by real rules. To Dahl, a ruling elite only exists when a well defined minority group becomes dominant, such that the preferences of the dominant group prevail over the rest of society. He contends that, in this form, there is a testable proposition for a ruling elite theory, but is critical of Mills and others establishing a quasi-metaphysical theory of elites, one where there is an endless sequence of underlying influences that cause apparently democratic behaviour to serve elite ends.

The primary issue at the heart of this dispute concerns how to treat preferences. Dahl's approach does recognize that preferences of the masses may, within some range, be modified in a way that serves elite ends. His test for elites takes preferences as given. On this basis, it is relatively easy to suggest that so called elites are not 'elites' in any meaningful 'outcomes' sense, and represent pluralistic interactions as the outcome of representative processes which are fundamentally democratic. However, when preferences expressed in political and social form are endogenous, it is appropriate to consider whether there are systematic ways in which elites modify preferences. Nevertheless, Dahl's critique was effective in drawing attention to the metaphysical undercurrents of Mills approach and the apparent inability (or lack of inclination) to provide verifiable specifications of elite relations.

The debate between pluralists and proponents of the power elite was monitored by scholars who adhered to the Marxian notion of the ruling class and the associated issue of class exploitation and the role of the state in this exploitation. The consensus was that there were deficiencies in both approaches. The Marxian critique of pluralism centers on the atomistic interpretation of social action adopted by pluralist scholars. The main concern was that

elite theory, particularly that associated with Mills, substitutes elite stratification for a structural representation of society based on conflict and contradiction between elites and non-elites, underemphasizing the contradictions of class conflict (Balbus 1971).

The consequential discussion between the power elite theorist, pluralists and Marxists has important implications for the development of policy. The power elite theorist conceives policy as a process that has been effectively centralised by the interlocking of diverse functional elites, be they in politics, bureaucracy, industry, the military, the media, labor organizations, business organizations or 'think tanks' linked to any of these functional groups. The interests of non-elite elements are seen as being the subject of tokenism. Marxist, and to some extent classical elite theorists, see the dominance of a ruling class as imperfect and subject to constraint. To Marxists the constraint is due to the internal contradictions of capitalism. To the classical elite theorists, the constraint is due to competition from alternative elites and the range of activities that mass society will reject as illegitimate, immoral etc. The pluralists, however, consider the policy process as a mechanism whereby diverse, and specialized interests, are organized. The consequent specialization of policy making reflects a practical mechanism through which the policy process is decentralized, permitting the resolution of issues through compromise and negotiation in a manner that serves majority interests.

Since the 1970s, there has been a relatively steady stream of literature associated with elite theory. It became a staple subject in comparative politics (Robert Putnam 1976) and emerged as a school of thought in sociology (John Scott 1991). The major scholars working in this field include John Higley and Eva Etzioni-Halevi.

In addition to considering elite theory itself, Higley has undertaken notable survey investigations, including *Elites in Australia* (Higley, Deacon and Smart 1979). The focus of his surveys has been on identifying policy elites in public service and politics, their networks with elites from other sectors and consequent influence on government and on the public. Importantly, diversity and division within elites is a significant aspect of his work. Etzioni-Halevi has given attention to the structure of elite theory, focusing on the problems of elites and the potential that elites provide democracy and the process of democratization (1993). Like other modern theorists, she has introduced multi-tiered social stratification into her analysis, replacing cruder analysis based on the classic elite and non-elite dichotomy.

### **Elites, Think Tanks and Policy**

Elites have now become commonly associated with policy development. Given the rise of think tanks, and their role in public policy development, the elite characterization of policy development is probably to be expected. In the United States, for example, policy is influenced by a range of social, political and policy think tanks (Family Research Council, National Center for Policy Analysis, Freedom Forum, Progressive Policy Forum, Centre for Public Integrity); economic think tanks (Competitive Enterprise Institute, Cato Institute, Economic Strategy Institute, Economic Policy Institute); and foreign affairs think tanks (International Institute for Strategic Studies, Washington Center for Near East Policy, Council on Foreign Relations, Centre for Defense Information). Many U.S. think tanks, such as the Brookings Institute, American Enterprise Institute and RAND, actually comment on a range of policy areas. Richard Haas (2002), Director of Policy and Planning at the U.S. State Department, has found that foreign affairs

think tanks contribute to policy development in five main ways: by generating “new thinking” on policy issues; providing experts who can work in public administration; providing fora for professional foreign affairs analysis to meet and discuss issues; bridging differences between parties; and encouraging public debate. These five points can be extended equally well to think tanks in other fields.

The fundamental issue here is whether these five contributions to policy enhance the responsiveness of policy development to public preferences, or simply facilitate the demands of interest groups seeking to influence public preferences. The public perception, on many issues, is that there is a divide between the wisdom of the common person, which is not reflected in policy, and the view of elites, which is reflected in policy. This can be readily illustrated by the issue of ‘political correctness’, which has been rejected by many as the product of intellectual elites (sometimes called ‘social engineers’) who lack the good sense of the common people who are governed by practical considerations. In view of this perception, it is now common for one side of politics to assert that the policies advocated by its critics are ‘elitist’, while their own policy pronouncements are grounded in good common sense. It is this ‘gap’ between elite policy views and public opinion on policy, and the attempts by elite groups to narrow that gap that is central when considering the influence of policy elites. For example, Higley and McAllister (2002) have used elite theory to consider why Australians voted against the 1999 referendum to replace their monarchy with a republic, when public opinion clearly showed that a republic was the preferred option. In spite of division among diverse elites, they found that some anti-republican elites were able to successfully associate a vote for the republic

with severing ties with the United Kingdom, which influenced many republicans to alter their voting intention. Similar research in Europe has examined the divergence between elite opinion and public opinion on European integration (Hooghe 2003).

## **Governance**

The concept of elites has been used recently to investigate the relationship between governance and economic growth. Having established that good governance and growth are not always positively related, World Bank researchers Daniel Kaufmann and Aart Kraay (2002) contended that elites have the potential to distort and even offset the influence of governance on growth. In their empirical investigation, the quality of governance was measured with respect to the likelihood that a government will be selected and replaced by constitutional and non-violent means; the likelihood that a government will implement policies that have general community wide benefits; and the extent to which individuals and social entities have confidence in, and abide by, the laws of society. A policy implication from their research concerns the issue of corruption and the relationship between international economic organization and developing countries. In circumstances where governments in developing countries have corrupt relations with economic elites, actions designed to improve governance arrangements may not necessarily improve economic outcomes, at least not in the short term while the vestiges of corrupt elite relationships remain.

From a more general perspective, to the extent that governance of political institutions is designed to enhance responsiveness to public demands, the goal of good governance is to reduce the gap between elite policy programs and public opinion on what constitutes good policy. In this circumstance, pluralists will suggest that rules are

preeminent. If the rules are correct, the policy process necessarily considers community demands and the outcome is necessarily representative. Schumaker (1991:203) suggest that pluralists seek three sets of rules for representative policy development. Policy makers must: (i) be determined by contested elections (polyarchy); (ii) welcome the participation of opponents in political processes and treat their claims as 'legitimate'; and (iii) accept decisions of law. Within this context, governance needs to provide transparent and accountable policy processes, so that contests and debate at all the three levels above can be effective. In contrast, the power elite view of policy is too pessimistic to offer meaningful insights on governance principles. Nevertheless, classic European elite theory and more pragmatic modern approaches to elite policy recognize that governance arrangements can further constrain elites when their policy view is contrary to public opinion. While the rules advocated by pluralists may provide legitimacy and accountability in a manner that reduces elite influence, rules alone are not the full answer as they do not consider the decentralisation of political decision making processes. In this regard, a highly centralized political decision-making arrangement is less likely to be responsive to community policy opinion than a highly decentralized arrangement

As a consequence, transparent and accountable public institutions appear to be well complemented by constitutional rules that provide for political decentralisation of decision making. This should have two important effects: diminishing the impact of policy elites on policy development when this is contrary to public opinion; and reducing the opportunity for elites to manipulate public opinion using public means. With decentralization, there would be more levels of government to influence, with the resulting

mixed messages constraining elite attempts to manipulate preferences. Of course, there is no suggestion that elites will disappear because of constitutional design and governance arrangements that emphasise accountability, but the gap between elite and popular views can be bridged by such arrangements.

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## Policy Networks

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### **Introduction**

Public policy and public administration in large urban settings face many challenges: the nature and impact of population growth, increasing demands for a wide variety of governmental services, pressures for expanded highways, improved response time of safety-related services, the growing need for increased supplies of water, the need for clean water, the challenge of controlling pollution, the increasing economic gap, the always present tension embedded in race relations, and so on. In addition to the formal arrangements of governments, many different kinds of networks (governmental, quasi-governmental, private, non-profit and volunteer) are forming and responding to various urban pressures and there is evidence to indicate they play an increasingly vital role in the design and implementation of public policy.

Because networks of public and associated entities are forming and influencing the implementation of public service, some profound questions need to be addressed. Namely, who controls these networks? Who is accountable for the actions of networks? Do citizens have access and exercise authority over the design and management of networks? Are networks a product of professional intent or epistemic behavior (Haas 1992)? What happens in networks, what determines influence within networks (Knoke 1990)? While not new, the proliferation of these relationships, have led several scholars to observe that “policy networks” are tantamount to a new form of governance (George 1999). What we know and have learned about policy networks is the concern of this article.

This article first attends to the evolution of the term “policy networks” and how the term has been used to depict influence in policy development. This section includes the definitional characteristics of networks. The article next examines a number of implications of policy networks, including the management and performance of policy networks. A final note on how governance and urban complexity are linked to the emergence and proliferation of policy networks in urban settings. By way of introduction, the suggestion is offered that urban settings represent conditions of complexity that develop corresponding organizational structures (networks) in response. The connection between condition and response is only suggestive in hope that further thinking about the emergence of networks can be examined. The point is that contextual matters do shape organizational energies and responses guided by various public leaderships. Yet, one can conjecture that there may be multiple reasons that give rise to the formation of networks.

### **Evolution of Policy Networks**

Networks have emerged for various reasons and can be viewed as responses to complex conditions. What are networks? At the broadest level, Hugh Heclo identified an “issue network” as a rather large set of actors in a given policy arena each seeking some power and influence within the network area (Heclo 1978). Such a network includes a variety of competing interests that shape the direction of public policy formation. This notion of issue network is similar to what other authors refer to as “policy subsystem.” According to Schroeder et al (1997:34) “policy subsystems ... are subsets of the larger political system”. Both networks and policy subsystems refer to a rather large set of actor relationships that have very complex patterns of interaction. Yet other authors have used

the term “issue system” to refer to yet another characteristic of a particular policy arena: the context of the intended policy choice (Sullivan and Meek 1997).

In the field of policy studies and public administration, the term “policy network” has been developed to refer to, “the relatively stable relations between (different) governmental and (semi-) private organizations in which processes of policy making take place” (Kickert et al 1997). Here policy networks are much more definable entities within the larger policy subsystem. The most instructive definition and incisive review of the literature on policy networks can be found in the work of Fox et al (1997). These scholars have focused on the familiar concepts of “iron triangles” or “cozy triangles” acting as some form of sub governments where policy making is determined by dominant players and economic interests (Cater 1965). The result, using a phrase from Fox and Miller, is a “theft of sovereignty!” Policy networks rob citizens of their right of policy direction and choice all subjugated to an informal policy making system.

In summary, scholars have identified the existence of “issue networks” (also referred to as policy subsystems) that contain a variety of actors each seeking some policy influence. Within these policy subsystems, one can also identify various “policy networks.” Policy networks vary in size and scope and influence. One can identify “iron triangles” as an example of one of these networks. Each of these policy networks can be examined as a political network: an association of individuals that are influenced by the social structure of the network. A policy network refers to *structures of interdependence involving multiple organizations or parts of organizations* (O’Toole 1997). Here the focus is placed on network relations and how these relate to accomplishing various kinds of tasks

(policy, political, functional). The chief characteristics of this definition are: (1) more than one organization is involved in a network; (2) network members perceive some interdependence as a result of involvement in networks, and; (3) that there is some sort of identifiable structure to the network. In addition to these characteristics, Marsh and Rhodes have offered a typology that differentiates between two very different types of policy network: the policy community and the issue network (Rhodes 1992) where a policy community is a particular type of policy network where a long-term relationships and shared norms have been developed among its members. These communities are differentiated from issue networks, similar to those identified earlier by Helco, which are characterized as a larger number of actors with variable degrees of commitment and dependence within a particular policy issue.

### **Implications of Policy Networks**

A central point with regard to the advancement of policy networks is how they influence both policy development and policy implementation. The idea that citizens are represented in policy deliberations and that neutral servants carry out policy decisions is a less-than-accurate betrayal of the functioning of political systems. Policies are determined and implemented by networked connections among mutually dependent participants. The network is the system! As a result, scholars have identified both governance and management implications with regard to the dramatic rise policy networks. With regard to governance, several concerns can be identified. For some, policy networks warrant much attention, not only from the “input” side of policy creation (or political demands) but from the policy “output “ or implementation side as well. Here again, the work of Hugh Miller is instructive in that his

work identified an emergent characteristic of policy network (implementation) as administrative discretion (Miller 1994). Miller warns us of “political activism” or even political professionalism by civil servants working in policy networks which challenges the assumptions made by “progressive” public administration built around the principles of hierarchical control, scientific management and neutral competence. Of central concern is the influence--by public administrators and those who support their goals and objectives--that takes place within these networks, especially in there areas where citizens are reliant on a professional bureaucracy and technical information that leads to a form of “technical rationalism” (Fischer 2000). Of consequence here is the lack of concern for involvement of citizens in determining policy decisions and the failure of policy makers and public administrators to embrace “democratic knowledge” (King & Stivers 1998:15) that is necessary to policy administration.

These concerns have lead others to examine policy networks as “political networks,” a term used to refer to observations within networks and the political structure of networks in general. These observations focus on the structure of relations within networks with a focus on power and influence within networks. The goal of this research is to develop a general theory of power in networks (Knoke 1990). The proposition is that an individual can be strategically situated in the network and can influence the patterns of exchange favorable to overall goal achievement. Power or influence is, as a result, a function of network position. Individuals or organizations that are situated in the center of the network are assumed to be more powerful than those who are situated at the periphery. Network analysis provides various “centrality measures” that may be used to determine an

actor's power. Networks can also be viewed from various viewpoints--from within the network (the net rider), from above (the net thrower) and from the side (the net puller)—in order to assess the various meanings of network operations. (LaPorte 1996).

In this light, Laurence O'Toole reviews the role of bureaucracy and the emergence of networks in relation to the central democratic political norms of responsibility, responsiveness and enhancement of political deliberation, civility and trust. He finds that networked public administration posses many challenges, yet the lessons of such a status provides “both complications and opportunities to facilitate parts of the democratic ideal” (O'Toole 1997).

Finally, the work of Myrna Mandell indicates the formation of policy networks and collaborative relationships are clearly the function of necessity: resource scare environments contribute to public administrators seeking joint solutions across jurisdictional boundaries (Mandell 1999). One can also imagine networks developing in non-urban settings like rural communities. In fact, networks are designed for rural settings, as in other settings, in order to link resources in a resource-scarce setting. One rationale for interagency networking in rural settings is the notion of “epistemic community” where like-minded networks of professional link resources to carry out missions deemed appropriate for a common area of service. Examples for this occurrence can be seen in the work of H. Brinton Milward and Louise Ogilview Snyder (Milward 1990). This essay stresses examples both of single and joint organizational productions of government services and how technology has replaced structure in the provision of government service, all of which lead to understanding government as a “hollow state.”

In addition to the concerns listed above, recent research on networks indicate that they



can also have a dark side (Raab 2003). Jorg Raab and H. Brinton Milward examined drug cartels, terrorist networks, and arms smuggling rings as “dark networks” that share the same characteristics as “positive” or legal networks. Their work reveals the rather pervasive nature of networks and the need to examine not only how networks function, but to whom they are accountable.

With respect to network management, the focus of much of the literature centers around two areas concern: management skills and network performance. Because networks are fluid connections of various types of participants, managing public networks will rely on different skills than those developed in hierarchies. Hierarchical control--all quite effective with traditional organizational systems--is clearly inappropriate when studying or managing a complex system. Public administrators are focusing their attention primarily on complex systems and self-organization—networks—that appear to be one solution or at least one possible property of a complex system (Douglas 1994). Others have examined a new set of skills necessary to be effective in the management of policy networks. The absence of hierarchy has made fundamental skills of public management (POSCORB) give way to a new set of skills that advance administration among multiple parties, including facilitation, framing, mobilizing and synthesizing. (Agranoff 2001). Robert Arganoff examined several policy networks in order to derive some basic lessons in the management of networks. His findings indicate that success is dependent of the skills of creativity, sharing burdens, facilitating agendas and flexibility. These skills, while evident in contemporary bureaucracies, seem necessary in managing policy networks. Meier and O’Toole found that managers who have greater interaction with environmental actors that are not direct line subordinates or

superiors had a significant impact on program performance and were able to influence program results (Myer 2003).

As discussed earlier, accountability and performance of policy networks are also of concern. It would seem that accountability in policy networks are at best elusive, and at worse, non-existent. One can image a continuous round of finger pointing when it came to public review of policy network services. Here the work of Provan and Milward is instructive. They examined publicly funded health, human service and public welfare organizations from three levels: community, network and organizational/participant. As La Port indicated earlier, each of these levels can interpret the network with very different goals and effectiveness criteria. The authors found that while “service-delivery networks must be built and maintained at the organizational and network levels, overall network effectiveness will ultimately be judged by community-level stakeholders” (Provan 2001).

One can easily visualize urban areas as a web of multiple and often-competing policy networks and jurisdictions covering a complex set of overlapping issues. For example, in the Los Angeles County alone, there are almost 10 million people living in 88 cities, with various regional councils of governments, regional associations, and countless special districts. This is truly an urban web that resembles a complex system. This complex system has overlapping mandates and actions can be interpreted in many ways: multiple truths and contrasting interpretations will exist. Complex systems turn out to have several fascinating but frustrating characteristics (Rhodes 1997).

## **Conclusion**

This article has attempted to make two points. First, networks have emerged for various reasons and in urban settings they have

emerged as a result conditions of contextual complexity. Such complexity has spawned newly formed associations (networks) to enhance professional and political associations and deliver services. Second, the various types of networks present some interesting challenges for public administration and public management.

Policy networks incorporate many organizations and are not typically governed by some sovereign. Formal network participants are involved frequently in the network and spend much of their time and resources in the networks (informal network report less involvement

Are these networks an emerging form of governance? Can these networks be self-organizing, inter-organizational networks, which have no sovereign authority and are operating independently from formal governmental structures and designing or negotiating their own rules for interaction? Rhodes may be accurate when he says that these networks are “inter-organizational linkages [that] are the defining characteristic of service delivery” (Nevell 1997).

How these networks are held accountable, and to whom are powerful questions within this emerging dynamic of networked public administration. It would seem that much of the judgment about the impact of networks as to how they influence the implementation of public policy will rest on the nature of each network and each network has the potential to be benign, descriptive or positive. If there is some evidence of such occurrence, we will need to review how such influence takes place and understand its value within the larger norms of democratic governance.

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### **Introduction**

Policy studies is one of those amorphous terms that mean different things to different people, but common to the different meanings is the generic concept of public policy. Or as Stuart Nagel (1988) suggests, the “field of policy studies can be broadly defined as the study of the nature, causes, and effects of governmental decisions for dealing with social problems (p.xv).” By “nature”, he means the political, social, economic, and/or cultural context in which the policy is being framed. By “causes” he means statistical determinants and policy formulation and implementation process. And by “effects” he means impact analysis and evaluation. In its simplest form, public policy can be defined as an officially expressed intention backed by a sanction, which can either be a reward or punishment. Policy, in other words, constitutes a mode of expression and action by the state.

The problem with this definition is that it is too mechanistic. Public policy has to mean much more, especially in a democratic society. Deborah Stone (1988) best defines policy as being “about communities trying to achieve something as communities (p. 14).” Public policy, then, can be said to reflect the collective aspirations of the political community, and generally formulated in the name of the public interest. This, of course, means that contained within public policy is some consensus of what constitutes the public interest. Policy studies, then, enable us to understand just what a community is trying to achieve. Moreover, through policy studies we can learn much about a community’s politics, ideology, culture, and underlying public philosophy, because policy studies can also tell us much about a society in terms of its

values and priorities. As Douglas Ashford (1977) suggests, policy studies perhaps ought to be conceived of as an effort to understand major political changes in the modern state. He specifically defines policy as a broad concern with how the state organizes itself to address new problems. Moreover, by comparing policies across national borders it then becomes possible to elucidate the differences between nations.

Policy studies, then, refers to approaches that are taken to the examination and evaluation of public policy. In this essay, I explore the problems that arise in contemporary policy studies, especially in attempting to strike the balance between community values and so-called neutral measures predicated on scientific methodology. While it would be convenient to develop one model of analysis and apply it to different situations, that would only fail to take into account differences between societies. Herein lies the key problem—that policy studies, contrary to a common conception of neutrality, is very much a political process, as well as a cultural artifact. This also means that all phases of the policy process are political.

Defining a problem is often a function of competing values systems that get played out in the political arena. Adopting a plan and implementing it is affected by the influence of competing interests and very much relies on strong political support. Evaluation too becomes a political process because benchmarks used to measure success are also a function of political interests and the extent to which social science research that buttresses a claim if utilized is also a question of whether they further a particular set of interests. Moreover, these processes only vary from nation to nation because of economic, political, and cultural differences.

This essay is divided into six sections, which when viewed as a taxonomy shows

that policy studies, when considered in terms of their various dimensions, ends up being a very political enterprise. The first section looks at the origins of policy studies, as first defined by Harold Lasswell within the mold of the policy sciences. This inevitably leads to two major themes in policy studies: traditional policy analysis predicated on neutral scientific measures v. policy analysis based on values. Section two examines the viability of the traditional model predicated on rationalism, and section three looks at the role of values in policy and the extent to which policy analysis needs be culturally specific. Related to the issue of values is the issue of whether policy studies can fit into a democratic framework. Section four then considers the policy process and the extent to which it is grounded in social science research as opposed to politics. In section five the issue of implementation is considered, and section six looks at the area of comparative policy studies.

### **Origins of Policy Studies**

Policy studies is thought to have originated with Lasswell and his conception of the policy sciences. Lasswell (1965) famously defined the policy sciences approach as analysis that effectively mobilizes intellectual resources to meet the challenge of great and continuing problems of the age. The policy sciences model, however, isn't merely what its name suggests—the use of rigorous scientific tools, though it certainly does employ them—but the rigorous analysis of a specific issue within its larger context. To take a policy sciences approach is essentially to take a contextual approach to the problem in question. “It examines the interplay of values and institutions, and the several phases of policy; it makes use of all techniques of data gathering and processing and adopts various methods...to its needs; it contributes to the strategies available to the achieving of

such overriding goals as the realization of human dignity—such as, for instance, the strategy of individual initiative. The policy sciences use policy for knowledge, and knowledge for policy” (p.33). As Lasswell (1951) put it: “the policy sciences are advanced whenever the methods are sharpened by which authentic information and responsible interpretation can be integrated with judgement (p. 4).” Therefore, a policy sciences approach is more interested in reconstructing the practice of society, which might also imply an interest in the assembling and evaluation of knowledge from whatever source in addition to simply knowledge about the policymaking process.

According to Michael Marien (1992), Lasswell's vision of the policy sciences was notably broad in scope. For him, the emerging policy orientation was twofold: the first part was to be directed toward the policy process, and the other was to be directed toward the intelligence needs of the policy. Lasswell took the view that the policy scientist was to be problem oriented and would be able to clarify goals. Building on that Yehzkel Dror (1971) defined the policy sciences enterprise as a new supra-discipline with the main concern of understanding and improving societal direction, focused on the macro-level. The policy analyst should not be a narrow minded technician, but a new type of professional—an “expert in generalism”—who deals in a broad, innovative, and open-minded way with problems. Policy sciences involve breaking down traditional boundaries between disciplines, especially between behavioral and management sciences. Knowledge must be integrated from a variety of branches of knowledge into a supra discipline that focuses on policymaking. In this vein, the policy sciences bridge the usual dichotomy between pure and applied research. For Dror (1983:8) developing the policy sciences is about significantly

improving the quality of policymaking. To that end, he describes it as the discipline which searches for policy knowledge “that seeks general policy-issue knowledge and policymaking knowledge, and integrates them into a distinct study.” A major component involved with the improvement of the policymaking system is how to increase the role of policy-issue knowledge in policymaking on concrete issues. If democracy is to survive in its competition with other forms of government, it cannot lag behind in using new knowledge.

As much as this was supposed to be the ideal, policy studies, as they have evolved, and the type of policy studies published, have fallen short of this ideal. According to Marien (1992), despite the remarkable growth in the scope of policy studies, Lasswell’s idealistic vision for policy studies has not been realized. Lasswell had actually stipulated that policy studies ought to be global in perspective, but nearly all American policy studies, as found in his review of some 420 active future-relevant and largely policy relevant journals, are devoted to domestic problems. Among the more glaring omissions in contemporary policy sciences is the lack of attempts at outreach. Lasswell advocated continuous general participation. As Marien puts it: “The academic core of policy studies generally lacks a systematic view, a sense of social change, an appreciation of the full range of alternative perspectives and options, a global perspective, an interest in technology change, an acknowledgment of environmental problems, and an interest and/or capability in outreach to a broader public” (Marien 1992:465). On the contrary, much of policy studies has tended to follow a more traditional path of analysis grounded in the social sciences, and most studies are what Marien refers to as “rewarmed social science.” Or as Anne Schneider and Helen Ingram (1997) note, the unifying theme

among the various approaches within the policy sciences framework is that policymakers will be able to solve problems on the basis of information obtained from policy analysis done on the basis of scientific procedure and according to scientific standards. By appropriate scientific standards is often meant the principle of instrumental rationality, which tends to be characteristic of the traditional model. And yet, that these scientific standards should be situated within context implies that policy studies encompasses much more than the traditional model.

### **The Traditional Model and its Problems**

Traditional policy analysis assumes the following elements: 1) goals and/or objectives can be defined; 2) alternatives to achieving defined goals and/or objectives will be identified and systematically weighed against one another. In the process of weighing, there will be a cost/benefit analysis that through statistical methodology will be able to show given a particular cost how much is actually achieved; 3) a decision will be made as to which alternative is to be selected; and 4) an evaluation of the policy to determine whether the chosen alternative was actually successful in achieving the stated goals (Nagel 1988). The traditional model, sometimes referred to as the “stages heuristic” (Jenkins-Smith & Sabatier 1994), as it is often called, assumes that analysis follows a simple flow chart and that the mechanics of the analysis are more or less straightforward.

The traditional model in large measure represents an ideal for purposes of guidance, but an ideal which often fails to be achieved in the real world. This tension is reflected in Charles Lindblom’s (1959) distinction between the root model—a comprehensive model—and the branch model, which is one of “successive limited comparisons.” The root

model is essentially a rational actor model and assumes that policy is made from the ground up. The policymaker defines the policy objective, carefully evaluates each alternative policy that could be chosen to achieve the stated objective by weighing benefits against consequences, and carefully chooses the alternative that best achieves that objective in the most efficient manner. In the branch model, everything is relative and choices are ultimately made on the basis of what is possible, not necessarily what would be most desirable were this an ideal state. The branch model is more realistic because it takes into account the complexity involved in formulating policy in a world where everything is ultimately contextual. This model is often referred to as the science of muddling through or incrementalism, whereby policy is often no more than an adjustment of what already exists, which only creates a new foundation upon which to build through incremental steps. And yet, even recourse to the branch model out of political necessity then relies to some extent on the root model to at least formulate the goals to which the policymaker will strive.

Nevertheless, Lindblom's distinction also reflects the tension between policy studies as a scientific enterprise and policy studies as a political one. The traditional model is in large measure predicated on a model of rational activism that assumes that once the goals of society have been identified, the choice of correct policy will necessarily flow easily so that society will be able to achieve the optimum social benefit (Johnston 1991). As the essence of rational activism is reason, it is further assumed that facts and values can be separated and that this separation will be rigidly adhered to (Downs 1991). The separation is predicated on positivist assumptions that value judgements are essentially emotional responses to life conditions. Because they are subjective, they

cannot be verified, and the purpose of rational choice is to substitute reason for arbitrary personal decisions (Fischer 1980). Whereas values are perceived and therefore cannot be observed, facts are and can be. This fact-value dichotomy has also served the traditional policy-politics distinction at the heart of public administration. As the objective is to separate politics from administration, the analyst has been able to effectively remove him/ herself from politics because politics is replaced by knowledge (Torgeson 1986). The question for the analyst is whether the policy works, i.e. does it achieve its goals, and as such s/he is able to maintain neutrality in evaluating policy by producing impartial results. By concentrating on the simple question of whether it works, the policy analyst avoids the larger and more subjective questions of which groups will benefit and which ones will lose, and whether such benefits are justifiable, let alone even desirable.

As a consequence of the fact-value dichotomy, policy evaluation has effectively been removed from public discussion. Public discussion, by contrast, violates the sense of appropriate isolation. Because administration and policy, and its subsequent analysis is bureaucratic, the structure of bureaucracy naturally militates against what Max Weber considered to be value rationality—the means by which the ends would be attained (Warren 1988). To introduce value rationality into administration is to bring about inefficiencies. The effect of all this is to make policy analysis a technocratic process, which by and large characterized the pre-policy sciences approach to policy studies. Herein lies the problem with this approach, especially when analysis is removed from the laboratory setting and then situated in the real world laden with politics.

Another fundamental problem with relying on technocracy is the complacent belief that

comprehensive analytic models are available that can then be applied to different sets of circumstances. Neutrality dictates that a universal set of measures be devised that can then be applied to all situations, regardless of specific differences, such as culture and underpinning philosophic foundations. Overlooked is that policy formulation is in most cases a response to the specific needs and circumstances of a particular community. Moreover, it ignores the reality that politics, especially in a democratic society, and one fraught with interest groups like the United States for instance, plays a major role not only in the formulation of policy, but its implementation and evaluation as well. As Barbara Ferman (1990) notes, American politics is specifically coalition politics, where the need to forge broad coalitions out of many diverse factions means that policy must have broad appeal. This can no doubt be accomplished through the use of vague language, the endorsement of broad goals, or a wider dispersion of resources. But in attempting to achieve this broad appeal, the goals often lose their conciseness. The traditional model also misses the fact that information supplied by so-called neutral agents will also be used for partisan politics. That is, contrary to the assumption that policy analysts may be empty vessels, they are individuals who are socialized and come to particular problems with their own individualized values systems.

### **The Role of Values and Ideology**

The problem with the traditional model is that facts cannot be separated from values because facts are ultimately evaluated through the prism of value systems. Moreover, the dichotomy assumes that the policy analyst can evaluate in a vacuum, totally disconnected from a sense of social purpose. Public policy, however, is essentially a political arrangement “designed for the

practical world of social action where facts and values are inextricably interwoven” (Fischer 1980:2). Or as Stone (1988:14) puts it, public policy “is about communities trying to achieve something as communities,” despite the fact that there is often disagreement within those communities over just what those goals ought to be. Public policy generally reflects a consensus of what constitutes the public interest, and it would be very difficult to conceive of the public interest as some conception apart from some commonly held values. In the end, this means that on a very simple level when a policy analyst seeks to determine whether a particular program works, such as a welfare-to-work type of program, s/he does have to make a value judgment.

Although facts might well be out there, how they are interpreted will be affected by the value systems each analyst brings to bear. To the extent that we are all products of our environment, it is naive to think that the policy analyst has not similarly been socialized into a particular milieu (Weber 1949). Facts, then, aren’t merely facts, rather they are simply notions that we have all come to recognize in the same way through the process of socialization. And yet to take the position that there can be a separation is to acknowledge the non-viability of the social science model to the policy process, unless it is viewed as being in the service of the larger policy process. In this vein, the social science model parallels the politics-administration dichotomy characteristic of the earlier public administration literature, also predicated on the rational actor model (Denhardt 2004).

At issue in the role of values are the extent to which they should be factored into the analysis. This would appear to be important because value is an important component of the Lasswellian model of policy studies. Public policy should be measured against the criterion of whether it is working to foster a



civil society, and whether it is indeed consistent with the underpinning philosophic foundations of that society. Guy Adams (1986) frames this in terms of what he refers to as the *sensus communis*, which literally means “common sense” but also speaks to the larger cultural traditions of society. As Adams (1986:173) explains: “The *sensus communis*, then, in its descriptive mode, may be used as an essentially valuative framework to view ethical standards underlying the social and political practices and traditions of a community. In its normative mode, the *sensus communis* informs the valuative processes which are the base of those social and political practices”. The *sensus communis* in short reflects the community’s values and the ethical standards of the community based on those values.

Policy studies predicated on a valuative discourse would then require nothing less than the abandonment of the fact-value dichotomy in favor of a more serious discussion of community values. To do so would ultimately render policy studies consistent with the idealized policy sciences approach, that policy studies should serve the purpose of both improving policy making and bettering society. To the extent that this is true, it must consider more prominently the role of ideas. Robert Reich (1988:6) has suggested that policy making ought to be more than the discovery of what satisfies public desires; it “should entail the creation of contexts in which people can critically evaluate and revise what they believe”. The function of policy, then, is to engage the public in ongoing dialogue.

Paul Roth (1987) suggests that policy analysts adopt a more pluralist view of rationalist inquiry, what he refers to as methodological pluralism. This would entail pulling together different approaches on a more philosophical plane for the purpose of acquiring a more meaningful understanding

within the context of specific circumstances. In other words, methodology has to be culturally relative. Michael Quinn Patton (1978) refers to this approach as utilization-focused evaluation whereby the process of assessing the effectiveness of a policy requires taking into account the specifics of the circumstances. In short, no one cannon can be used in all circumstances, but that the general methods would have to be adapted to each individual set of circumstances. The implication for policy studies could not be more clear: the approach to policy studies in the U.S. has to differ from an approach that would be taken in Europe, Africa, the Middle East, and other parts of the world because of social, economic, political, and cultural differences. Ashford (1992), for instance, couches this as the need to place policy studies in context, and when comparing policies of one country to another one is ultimately attaching different contextual meanings.

At the same time, this is not the same as calling for an abandonment of scientific principles. John Dryzek (1990) suggests the “Q methodology” which requires that statistical analysis be subordinate to a broader analytical and interpretive task. The Q methodology is essentially an empirical approach to the study of human subjectivity. As Dryzek (1996:124) explains: “A Q study begins by modeling subjects in terms of their reactions to a set of statements about a given domain. Unlike more widely applied methods such as survey research, Q is not concerned with patterns across variables, but with patterns and across individuals.” In practical terms, when asking a respondent a series of questions, the answer to one specific question only makes sense within the context of all the questions in the set, which in terms of this methodology is referred to as a *Q sort*. The *Q sort* essentially represents a respondent’s orientation to a particular context from which

specific questions are framed. How a respondent answers a question, even on a simple survey, will be determined through the prism in which s/he approaches that survey. Aside from the fact that objectivity, does not exist, one's answer to a specific question cannot exist in a vacuum, rather it must always be in context. To generalize this methodology to policy analysis is to say that a specific policy must always be analyzed within the context of its specific societal context.

This in large measure brings us back to Lasswell's ideal of the policy sciences whereby rigorous scientific method be applied within broader social context. Paul Healy (1986) has suggested that we can make effective policy by improving our understanding of ourselves and our environment. This approach is similar to Duncan MacRae's notion of *act-utilitarianism*, whereby the application of expert knowledge is subject to the control of political responsibility. The object of policy analysis, and by extension policy studies, is to serve a broader social function. Therefore, it ought to "provide guidance to society, through research, reasoned discourse, and education as to what interests should be served in particular circumstances and as to the means to do so" (MacRae 1976:306). This, of course, requires no less than an examination of social values to see whether the ultimate goals of society are being achieved, because to talk about policy is to talk about the different ways in which the values of the community can be served.

Bringing back values requires recognizing the twofold nature of values inquiry. First, there are those values that drive the policy in the first place—goals. And second, there are the underpinning values of the community—those that mark its identity and form the cultural set of lenses through which policies will ultimately be viewed. To talk about a

society's values is to talk about that society's broad historical tradition. The goals of policy, then, need to be determined in light of those values, which would involve no less than a philosophical inquiry into the society's underpinning values. In measuring policy, the analyst would need to ask whether a policy has implications for the values and traditions of society (Levin-Waldman 1996). All of this goes back to Stone's definition of policy as that which reflects the collective aspirations of the political community. This also suggests that ideology has a role to play in policy studies. Therefore, policy framed according to ideology often asks the following question: to what extent does the policy at hand further the essence of the community's guiding ideology, or what we might refer to as the reigning public philosophy? To ask the question is to bring policy studies into greater consonance with democratic theory.

This feeds into yet another question in policy studies: to what extent are they elitist, and as such whether they can in fact further the democratic enterprise? Peter deLeon (1997:6), for instance, suggests that all too often important work in policy is the privileged domain of a policy elite, and not as Lasswell put it "directed towards knowledge to improve the practice of democracy." On the contrary with the rise of the policy sciences, there has been a deterioration in democracy, in large part because of a tendency to defer to expertise of the policy technician. As much as policy sciences might be a function of a utilitarian approach—to demonstrate that policy does indeed serve the interests of the greatest number of people—the over-reliance on traditional positivist methodologies for analysis only serves to distance the policy analyst from the policy recipient, i.e. the target population.

In other words, there may be a danger to society of privileging science and technology if the effect is to embrace other forms of

knowledge and decision making. Schneider and Ingram (1997:38) suggest that one of the problems with policy sciences, and by extension policy studies predicated on that model, is that it has not taken it as their responsibility to “educate citizens about policy complexities so that informed citizen judgment—rather than scientific expertise—can guide public policy. When science replaces the voice of ordinary people, it disempowers them just as much as any other form of elitism.” But this would be equally true for the policy analyst who uses his/her expertise to discover community values. On the other hand, this may well assume too much because the “professionally trained” policy analyst may not figure as prominently in the process as either of these models suggest.

### **Policymaking Process**

Dror (1983) has argued that the policymaking process is a very complex and dynamic process, in which different contributions are made through its various components. These components are interconnected by communication and feedback loops, and they interact in different ways. Policymaking in short is what he refers to as a species of decisionmaking. The policy sciences model holds that knowledge should serve to improve the policymaking process, which would then imply a supportive role for research—that the results of good social scientific research should drive the public policy process. It essentially provides the foundations for the evaluation of alternative courses of action during the choice phase of the process, as well as the foundations for doing cost-benefit analyses. Among the various themes in policy studies is the role played by research in policy formulation. To the extent that the traditional model is grounded in social science, it relies heavily on research. Policy made in accordance with a social science model would

be based on rigorous scientific research that could establish a causal relationship between the policy in question and the stated objectives. In this vein, the social science model only tends to view research as being indispensable to the process. In the idealized social science model research is indispensable to the process because, if nothing else, it reduces uncertainty and thereby provides a basis for choosing among alternative policy options (Levin-Waldman 2004).

Robert Rich and Cheol Oh (2000) maintain that the acquisition, dissemination and utilization of information is a positive activity that is in the interests of stakeholders, which would include policymakers and affected interests. One might expect, then, based on theories of rational activism that information, i.e. research, would be consulted to reduce uncertainty and provide a basis for choosing among alternative policy options. That is to say, once information is acquired it will be used, and that it will have an impact on the policy outcome. And yet, they found that when policymakers received more information, they were not necessarily likely to use it. On the contrary, individual decision makers do not necessarily process information in ways assumed by rational actor theories. Information processing is contingent on the specific policy area, and decisions are made on the basis of organizational interests.

Michael Cohen et al (1972:2) suggest that the best way to conceive of the policy process is as a garbage can into which various problems and solutions are dumped in by a variety of different actors, who themselves move in and out of the process. “The mix of garbage in a single can depends on the mix of cans available, on the labels attached to the alternative cans, on what garbage is currently being produced, and on the speed with which garbage is collected and removed from the scene.” In other words different people as

they move in and out of the process put different ideas into the mix and the outcome is not only affected by the mix within the can but by a host of variables outside the can, such as the types of pressures that different actors in the process are responding to.

Policy in its final form is often the confluence of policy streams and political streams that are able to take advantage of new policy windows. Policymaking is often the result of what John Kingdon (1995) refers to as a policy primeval soup. Policy communities composed of specialists in a given area tend to operate independently of political changes or pressure from voting constituents and interest groups. Independent of a specific problem or policy stream is the political stream that is composed of things such as public mood, campaigns mounted by interest groups, recent election results, ideological and party composition of legislative bodies and composition of the executive. Policy is made, however, when the policy and political streams have been coupled, and this usually occurs when a policy window is opened, i.e an opportunity arises that can really be taken advantage of.

### **Implementation**

One of the topics in policy studies that has been gaining attention has been the field of implementation studies. It is important because it underscores the political nature of the policy process, and also the political character of policy studies. In short, implementation involves understanding what has happened to a policy and/or program once it has been enacted. Most scholars assume that a reasonably clear distinction can be made between formulation/adoption of policy—usually in the form of a statute or landmark court decision—and its actual implementation by one or more administrative agencies. Implementation of any policy involves efforts of some

policymakers to affect the behavior of both those charged with administering a policy and the target population—those who are intended to be the beneficiaries. Dennis Palumbo and Donald Calista (1990) maintain that the field of implementation studies has been distinguished by two discoveries: First that prior to the discovery of implementation, its significance for public policy was largely overlooked. And second that implementation has been recognized to have an independent effect on policy outcomes.

Implementation, then, has to be understood as being part of the broader policymaking process, and that it has a relationship to other parts of the policy cycle: design, problem definition, formulation, and evaluation. Implementation is a complex process which involves more than simply the management of government programs; it involves understanding the conditions under which policy can be expected to be successful. Which is to say, that there is no one uniform model for policy construction and implementation, rather it has to be environmentally and culturally specific. What, then, determines whether or not a policy will be successfully implemented?

According to conventional wisdom, successful implementation occurs when 1) the policy correctly identifies the problem, which means that the enabling legislation or other directives that mandate policy objectives need to be clear and consistent and provide substantive criteria for resolving goals conflicts; 2) the policy contains unambiguous directives that organize the implementation so as to maximize the likelihood that the target population will behave as desired. Moreover, it has to incorporate a sound theory identifying the principal factors and causal linkages affecting policy objectives; 3) the enabling legislation has to structure the implementation process in order to maximize the probability that implementing officials

and target groups will perform as desired; 4) those implementing the policy possess the necessary managerial and political skills and commitment to its goals; 5) the policy is actively supported by organized constituency groups and key legislators and/or other public officials throughout the implementation process; and 6) the relative priority of the policy objectives, especially as they have manifested themselves in statutory form, are not undermined over time by conflicting public policies or by changes in relevant socioeconomic conditions that limit the policy's purposes or political support (Mazmanian & Sabatier 1989). In this vein, implementation is not purely a technical enterprise, but must be viewed as an exercise in continuous problem solving. Consequently policy failure may be as much a function of inadequate problem definition or policy design as administrative malfeasance or nonfeasance. And administrative failure could be viewed as stemming from the inattention paid by legislators to program constraints during the policy decision. Problems or failures in implementation are as much a consequence of flaws in the policy formulation process and in the environment in which implementation occurs, as they are to specific problems of implementation per se.

Implementors are involved at every stage of the policymaking process: agenda setting, problem identification, formulation, implementation, and evaluation. Polumbo and Calista (1990) suggest that when one opens what they refer to as the "black box" of implementation one discovers that formulation is only a small part of policymaking. On the contrary, much of policy is actually made during implementation itself. And it is for this reason that implementation is an important aspect of policy studies. Good implementation must demonstrate an awareness of the characteristics of the society in which it is to

take place. The implementation analyst must know a range of access points where formulation and implementation can influence the course of events; and s/he must also recognize which social and institutional factors in a specific implementation effort cannot easily be affected through present action. Those factors figuring into implementation analysis include: available resources, economic capacities, technological know-how, and prescribed (constitutional) political rules. According to Daniel Mazmanian and Paul Sabatier (1989) implementation has inherent dynamics that are driven by at least two important processes: the need for any policy that seeks to alter behavior to receive a constant or periodic infusion of political support, and also the need to achieve cooperation among large numbers of people.

Hank Jenkins-Smith and Paul Sabatier (1994) put forth the concept of the advocacy coalition framework (ACF), which is essentially a response to traditional policymaking along Lindblom's root model. ACF deals with policymaking change over several decades, and it consists of four basic premises. The first premise is an understanding of the process of policy change, and this requires a time perspective of a decade or more. The second premise focuses on policy subsystems, which involves looking at the interaction of actors from different institutions and how they seek to influence policy. The third premise focuses on the intergovernmental dimension, at least in the realm of domestic policy. And the fourth premise holds that public policies can be conceptualized in the same manner as belief systems. As they explain: "Within the subsystem, the ACF assumes that actors can be aggregated into a number of advocacy coalitions composed of people from various governmental and private organizations who share a set of normative and causal beliefs

and who often act in concert.” Belief systems of various coalitions are organized into hierarchical, tripartite structures, whereby higher/broader levels constrain more specific beliefs. At the highest/broadest level, the ‘deep core’ of shared belief systems includes basic ontological and normative beliefs. At the next level are the ‘policy core’ beliefs which represent the coalition’s basic normative commitment and causal perception across an entire policy domain subsystem. “They include fundamental value priorities, such as the relative importance of economic development vs. environmental protections.” In the end, then, policy studies that does not take into account the realities of the political universe and the competing values systems that often get played out in politics, will not be able to get to the core of the policy issue.

### **Comparative Policy Studies**

The argument of this essay thus far has been that inasmuch as policy studies tell us something about the character of a political system, and how that system addresses its problems and prioritizes its values, it tells us much about that system’s culture. It does this precisely because it must incorporate values. This would then suggest that a very important dimension to policy studies is indeed the comparative one. Already a policy sciences approach acknowledges cultural differences to the extent that it incorporates a society’s underlying philosophy into the policy process. The field of comparative public policy studies, however, isn’t fully developed. At the same time, it is important because a comparison of policies of different political systems—different countries—can actually tell us much about differences between political systems. Nevertheless, Arnold Heidenheimer et al (1990) define comparative public policy as the study of why different governments pursue or do not particular courses of action. Studying comparative

policy gives special attention to the effects of government’s actions on people’s lives.

Howard Leichter (1977) suggests that there are several obvious advantages to comparative policy studies. First and foremost, it may yield an important political dimension upon which to compare and evaluate political systems. The introduction of actual policy output and input data can provide a more complete and accurate basis for comparison and might even lead to some altered evaluation of the performance of these political systems. Comparative analyses can further enable us to generalize about the selection, content and consequences of public policy. The extent to which political culture and ideology, socioeconomic structure, or the nature of the political system affects policy can only be determined by extending policy analysis across national borders. Therefore, comparative policy analysis allows us to engage in quasi-experimental research. It enlarges the basis for comparison and the evaluation of political systems by allowing for a more conclusive testing of the relationship between public policy and various independent variables. And it also provides an opportunity to compare and evaluate the experience of different nations in attempting to find policy solutions to public problems. We are able to gain a deeper understanding of how government institutions and political processes operate as they deal with concrete problems. Policy strategies adopted in one country do often have important impacts on policy making in other countries, which only underscores the interdependent nature of the world (Heidenheimer et. al. 1990).

At the same time there are also problems associated with comparative policy studies. One is that the extension of the range of political, social, and economic factors encountered in cross-national studies involves too many variables which might make it

difficult to isolate those variables responsible for the selected policy. Another problem is that by comparing national level public policies there is the danger that significant intra-national variation will be concealed, thereby weakening the validity of cross-national comparisons and evaluations. Another problem lies in the tendency to assume as a given certain universal values which may not be cross-culturally acceptable to all societies. Moreover, there is the issue of the quality and commensurability of data (Leichter 1977). The successes and failures of other nations may not necessarily transcend national boundaries (DeSario 1989).

Dror (1983), for instance, suggests that the main difference between policymaking in democratic countries and dictatorial ones is that in the former private individuals and elected legislatures play a bigger role while in the latter legislatures tend to contribute almost nothing to the process. Policymaking in developing states tend to be characterized by what he calls a model of “pure” developing states or “avant-garde developing states,” which contain the following elements: They have very low technological development; they have a strong initial or communal structure that is slowly disintegrating; there is a mass leader and a small political elite that aspires towards rapid and radical socioeconomic transformation; there is practically no middle class; they have a long history of colonial rule, which ended after a period of militant nationalism; policymaking is wide in scope and tends to cover most economic activities. The basic characteristic of the policymaking process, however, is that it is often shaped by pattern that predates independence. Developing states do little conscious determining of policy strategies. On the other hand, the policymaking structure in developing countries is much simpler than in modern countries, as government bureaucracy in

developing countries tends to be weak. But most do have special planning units (Dror 1983: 105-120).

## Conclusion

This essay has attempted to show that when the various dimensions of policy studies are explored, it is ultimately a very political process. I have attempted to demonstrate this by beginning with the origins of policy studies as a scientific endeavor, and by showing how the limitations of each inevitably leads to a consideration of the next. Because of these various dimensions—themes—in policy studies, there really is no singular definition. What is clear, however, is that policy studies that only looks at policies per se without consideration of the contexts in which they are being framed and evaluated is insufficient. Policy studies must ultimately be able to tell us something about ourselves, our communities, and how our behavior may be affected. From problem definition through formulation, implementation, and evaluation, policy studies must take into account the underlying values of the communities in which they were intended to resolve specific problems. This, of course, can only lead to the inescapable conclusion that not only is policy studies an amorphous concept, it is also never a static one. As societies undergo change and transformation, so too do the processes of policymaking, thereby resulting in new dimensions to policy studies. In the end, this only makes the comparative aspect of policy studies even more critical, because the changes that one nation has undergone and its impact on policy have lessons for other nations that are also poised to undergo transformation.

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### **Introduction**

Politicians generally maximize the benefits of short-term gains that can be realized through elections. They are often considered to be myopic in their policy formulation and implementation. Macroeconomic policies are often the offshoot of dominant political considerations. Thus, the political economy of macroeconomic policy is an interesting and realistic area of study in macroeconomics. Fortunately, most economists have come to realize that good economic advice requires an understanding of the political economy situation and they are now doing this analysis explicitly, rather than implicitly as used to be the case a few decades ago (Rodrik 1996:38). Political economy argues that macroeconomic policy-making is the result of political struggle within an institutional structure and that policy-making is significantly influenced by political factors (Alseina & Perotti 1994:351).

The basic purpose of the present article is to pinpoint several cases by way of interpreting the areas where political rationality gets conflated with economic necessity in the shaping of macroeconomic policy in both developed and under-developed countries. Our discussion is divided into several parts. The introduction is followed by a discussion of policy-making. Section three is devoted to an explanation of political business cycles followed by an analysis of the fiscal deficit. This leads us to the analysis of market failure as well as government failure. Section six analyses the politics of privatization, while section seven explains political instability, exchange rate depreciation and inflation, and the last section of the paper makes some concluding observations.

### **Policy-Making: Rules Vs Discretion**

One of the critical working hypotheses of the new political economy is the view that government is basically inefficient and nothing should be left to its discretion. In fact, monetary or other crucial policies are too serious to be placed at the discretion of the government. Advocates of policy rules often argue that the political process can never be trusted. They have the strong belief that politicians use economic policies to further their cherished ends and that they often commit frequent mistakes in conducting macroeconomic policy.

Another objection to using discretionary policy is that it is often associated with time inconsistencies. The issue of rule vs. discretion becomes immediately relevant in the formulation of monetary policy which can be conducted through either rules or discretion. In this sense, the independence of the central bank becomes critical in many ways. The independence of the central bank is indeed a political matter. The legal independence of central banks can be measured by a number of indicators, including the power of the central bank governor; the independence of the governor in policy formulation; framing objectives; and also decisions of lending to Treasury. A number of factors are important in judging the extent of central bank independence in a country. These include the length of the term of office of the governor, the power of the executive head to recall or dismiss the central bank governor, the role of government officials in the Board of the Bank, the frequency of contact between the governor and the government, and so on. The independence of central banks can also be looked at from the perspective of the turnover rates of central bank governors. This perspective measures the average number of changes of governors per year. The index thus

prepared will be an actual measure of central bank independence. It can be observed that inflation rates are positively associated with turnover rates of central bank governors and negatively correlated with the central bank's legal independence.

Many studies find a negative correlation between the independence of central banks and the rate of inflation (Alesina 1988, Alesina & Summers 1993, Campillo & Miron 1997). A high negative correlation is found mainly in those countries where the central bank is kept away from political influence on monetary policy formulation. The real issue however, is how much political influence enters into policy-making? Whilst making policy or explaining a macroeconomic phenomenon, economists, having different degrees of political orientation or points of view, often agree to differ from one another. This is also true in the case of fixing the point of trade-off between two mutually conflicting objectives of macroeconomic policy such as price stability and full employment.

However, the decision to agree on a particular point of trade-off is, more often than not, political in nature. For instance, economists, providing research support to political parties or governments, are not free from political bias and partisan influence. A Republican president in the United States of America would prefer a situation of less inflation and perhaps more unemployment if a trade-off is to be found at all between the two. The situation is completely the reverse for a Democratic President of the same country (Nordhaus 1975:173). It has however, been empirically observed that some macroeconomic phenomena, such as inflation and unemployment, often occur in a cyclical manner, and this is supposed to be mainly due to political factors. This brings us to the issue of the political business cycle.

### **Political Business Cycle**

The theory of political business cycles is an important area of public choice theory, and clearly shows the close interactions between macroeconomic and political analysis. Ever since the publication of a paper by William Nordhaus (1975), the subject has become the center of attention not only among economists but also among political scientists and political economists (see, for example, Berger and Woitek 1997; Rogoff and Sibert 1988; Treisman and Gimpelson 1999; Hibbs 1977; Block 2002). The basic assumption of the theory of political business cycles is that politicians are guided mainly by short-run considerations. A ruling party wants to maximize votes and win the election. Therefore, before elections, it may reduce unemployment through expansionary monetary and fiscal policies. Since the voters are myopic, they do not have the ability to appreciate the long-run implications of such a policy. However, by following the expansionary policy, the party comes into power, but experiences, after a time lag, the emergence of inflationary symptoms.

Inflation after elections can occur in three main ways. First, there can be pre-electoral manipulation of monetary-fiscal policy that leads to tax cuts and monetary expansion to generate more demand. Second, the government, after coming to power, may prefer to raise the prices of products and services which are under its direct control. This may be due to motives such as the perceived need for a budget surplus, better command over resources and the financing of desired projects at hand. Third, during elections, the government gets financial help from business people, traders and producers with the tacit understanding that, if elected, these people can make up the loss by raising the prices of their products without any objection from the government.

In the model developed by Nordhaus, there is an implicit negative relationship between unemployment and inflation. The logic is based on the Phillips curve analysis. This implies that when unemployment goes down, inflation has to go up. In order to control inflation, the party in power activates tight macro-policies of less spending and budget surplus. But then, because of the negative relationship, inflation is brought down and unemployment increases. So there is a cyclical relationship between these two critical macro-variables, which gets accentuated by political factors. The cyclical ups and downs are also possible in general economic activity where upswings may be followed by downswings, and inflation may follow recession. This is found to be empirically the case in many countries.

In the generation of political business cycles, the central bank of a country may, to a great extent, be responsible, particularly when the latter is not independent of executive control (see, Leertouwer and Maier 2001). It is an established empirical fact that fiscal deficits show a general tendency to escalate in many countries during election years. The behavior of such deficits can be explained more or less satisfactorily by political economy factors.

### **Political Economy of Fiscal Deficits**

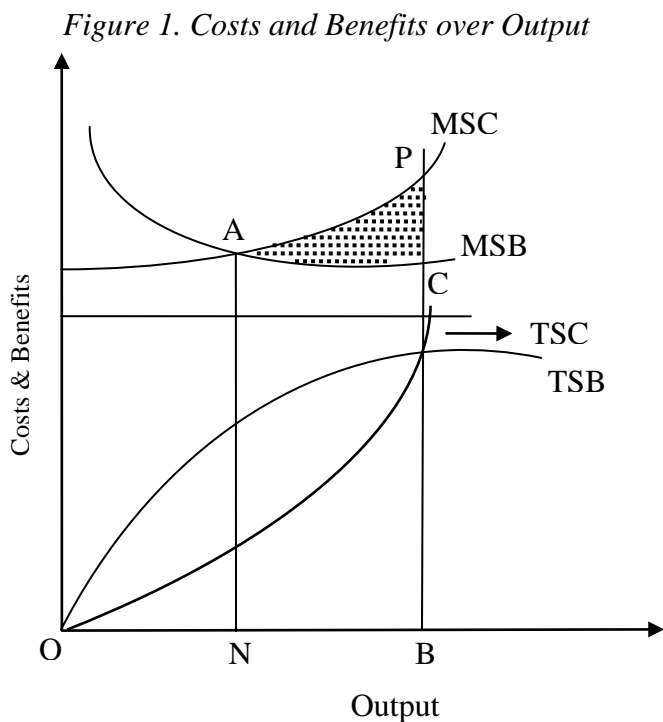
Persistent budget deficits in many countries during the 1980s and 1990s have encouraged many researchers to investigate the sources of deficit bias in fiscal policy beyond the domain of pure economics. One explanation provided by the new political economy suggests that governments are sources of enormous inefficiencies. They are engaged in rent-seeking activities and there are obvious regulatory failures in many directions. The bureaucracy is engaged in maximizing the budget and extravagant expenditure. Therefore, high rates of inflation and

persistent budget deficits are common factors in such economies. But the bad news is that fiscal deficits often reduce economic growth (Easterly et al. 1994).

In recent years, Max Weber's view about benevolent and efficient bureaucrats has been challenged by various authorities. Representative works on bureaucracy have been done by W.Niskanen (1970), among others. In fact, without understanding the influence of bureaucracy, the genesis and implications of the political economy of macroeconomic policy cannot be properly appreciated. In the Niskanen type of model, the bureaus have the following two essential characteristics (Ghosh 2001). First, bureaucrats maximize the total budget of their bureaus under given demand and cost conditions, subject to the constraint that the budget must be equal to or greater than the minimum total costs at equilibrium output. Second, bureaus exchange specific output for a specific budget. The starting point of such a model is that bureaucracy maximizes its utility function. The utility function subsumes many related variables such as salary, power, patronage, pecuniary motivation, easy management and so on. All these variables are a positive monotonic function of the total budget of the bureau. Thus, bureaucracy maximizes its utility function by increasing the size of the budget. The second characteristic – exchanging output for a total budget – gives the bureau the same type of market power as a monopoly. This is precisely so because the bureau is often the sole producer of a particular type of product which is sheltered from market competition (e.g., defense products). Thus, as a producer, each bureau is unique in its own way and enjoys some monopoly power.

Bureaucracy expands by increasing the size of its budget every year. This is possible because the government has to depend on bureaucracy; and its information base and

other details cannot be challenged by the government (minister). It should be noted that the relationship between a minister and bureaucracy is like a bilateral monopoly where settlement is to be made through compromise. Because of information asymmetry between a minister and a bureaucrat of a department, bureaucracy often enjoys a unique position as it possesses the stock of better and more up-to-date information. The proposed budget expansion by the bureaucrat is thus easily granted, and this results in inefficient output. See Fig. 1 below:



As the diagram reveals, the market efficient output is ON; but output under bureaucracy is OB which shows  $MSC > MSB$  i.e., a loss of efficiency (APC area). The sponsor grants the budget because he/she believes that maximization of output is good for vote maximization in the re-election. Generally, a minister does not annoy a bureaucrat and they are in collusion on many matters. Because of their monopolistic power, it is possible for bureaucrats to pursue rent-seeking behavior. However, there are mainly two types of inefficiencies in a bureaucracy.

First, there is allocative inefficiency arising out of output production beyond the optimum level justified by the equilibrium between MSB and MSC. The actual output production is inefficient because the cost is higher than the benefit. Second, bureaucracy involves X-inefficiency resulting from inefficient supervision, over-staffing, higher operational costs and so on. Thus, political processes in many of the DCs (developed countries) and LDCs (less developed countries) involve inherent deficit bias. Buchanan and Wagner (1977) argue that deficit bias mainly arises out of information asymmetry and misunderstanding of the actual situation. While the electors can well understand the obvious benefits of lower taxes and higher government expenditures, they are often ignorant about the implications and problems involved in expansionary fiscal policy.

In the making of fiscal policy, the interactions among the players may lead to different levels of fiscal deficit. These are: first, an elected leader may incur huge government debt to restrain his or her successor's spending. The desire to restrain future spending has been an important motive for Ronald Reagan's policy of high budget deficits in the 1980s. Deficits can also be used as important signals to tell voters about the ability of the government to enhance public welfare and social benefits. This was also one of the motives for Reagan's policy of high fiscal deficits. Indeed, signaling considerations may explain why politicians often use inefficient pork-barrel expenditure (expenditure to stay put in politics) rather than straightforward resource transfers to their cronies (Coate & Morris 1995). Also, the durability of government is a critical factor in explaining the quantum of fiscal deficit. In a constantly changing government apparatus, there is a likelihood of higher fiscal deficits (HFD) than in a government which is more secure, established and long-

lasting. The nature of governments also seems to matter in the creation and management of fiscal deficit. In a dictatorial regime, fiscal deficit may be much lower than in a democracy. However, in a 'benevolent dictatorship' things may be different. Also, the cost of running a democracy is probably higher than that of running a dictatorship.

A new government may also be more of a spendthrift than an old government. This is probably due to the implementation of new policies and new action programs. Thus, a new government will likely evolve a high fiscal deficit, and also the type of party in government may also be a decisive factor for fiscal deficits. A coalition type of government may have, more often than not, a fiscal deficit compared to a single party government. The nature of policy also matters in the case of a fiscal deficit. A government may try to solve one problem at a time. In such a case, fiscal deficits may be lower than for a government which tries to solve many problems at the same time in order to gain public confidence and politico-economic stability. A government that has to solve many problems simultaneously will likely be confronted by fiscal deficits. Some empirical findings are presented in more concrete terms in the discussion that follows.

Since cross-country differences in the debt/deficit ratios and fluctuations in fiscal deficits in many European countries over the years cannot be adequately explained by the known economic factors, the usual presumption is that some political economy factors must be playing a role. The Roubini and Sachs model (1989) shows that a weak and unstable government is associated with high fiscal deficits, and that a strong and stable government is associated with low fiscal deficits. Thus, political factors have a strong impact on budgetary balances.

From the available empirical studies on the political economy of budget deficits, a

few important lessons can be learnt (see details, Romer 2001). A country's political character plays a critical role in the budgetary outcome. Significant political factors are involved in the budgetary process, as well as the nature of any government coalition. It is necessary to understand the mechanism of how a plurality of power and its dispensation leads to the creation of budget deficits. It may be true that some strong political economy elements, other than mere changes in political guards, may be at work. Formidable fiscal deficit problems which were linked to government failure were associated with the debt crisis that affected a large number of Third World countries in the 1980s.

### **Market Failure vs. Government Failure**

Many Third World economies put emphasis on public sector regulations and controls. Most of these economies, which were freed from foreign domination and control, wanted to have more and more government control for many obvious reasons. The evidence of market imperfections and distortions in those countries gave the impression, in the minds of policy makers, that they were vulnerable to market failures.

The macroeconomic policies of these countries consisted of large-scale public ownership, strict controls over industrial growth, over-valued exchange rates and import-substitution. Each one of these policies has a political economy counterpart. These policies were designed to give more power to the government for centralization and industrial expansion under a protected environment. In addition, many countries followed urban bias strategies of development that seemed to strengthen the industrial sector through favorable sectoral terms of trade, withdrawal of rural savings, higher relative taxation on the rural sector and so forth (see, Lipton 1977). All these issues gave enormous power to the bureaucracy and led to

regulatory failures on many fronts. Currency values are generally looked upon as a symbol of national power and prestige. However, the adoption of the policy of over-valued exchange rates led to trade deficits that were unsustainably large. A large deficit can of course be financed by either foreign borrowing or monetization but both these measures involve financial instability (Rodrik 1996:14). Also, these decisions become, in the end, politically motivated.

In general, the fundamental problem of macroeconomic inefficiency and policy cycles in many countries arises out of distributional struggles among the contending partners or groups. The state is often an instrument in the hands of powerful groups and their possible coalition interests. Very often, the coalition governments in these countries want to retain their power as long as possible, and in doing so, they have to satisfy all the players in the game of politics. In every case, the governments have to satisfy the powerful groups that make and unmake the government. There is often a *war of attrition* between different groups, and the group that proves to be more powerful can capture the government. Due to a high degree of market imperfection, the market mechanism does not work in many developing economies. The invisible hand does not play any role, and instead, the visible hands of the state and bureaucracy operate more successfully in sheltering the economy from macroeconomic equilibrium. The existence of political markets in many LDCs results in misallocation of resources and is responsible for market failures (Ghosh 1998).

The political necessity of satisfying all classes of people for vote maximization in some LDCs, and the desire to stay in power, require the expansion of monetary-fiscal policy often beyond the justifiable limit. Domestic monetary and fiscal expansion, even by incurring public debt to satisfy

populist political motives, leads to persistent balance of payment deficits under the regime of fixed exchange rates (Krugman, 1979), and this ultimately makes the economy vulnerable to speculative attack. Conceivably, an expansionary macroeconomic policy will also mean raising wages and lowering competitiveness. Under such a situation, any attempt to defend the currency by the authorities will result in higher interest rates. High interest rates, increasing wages, deteriorating current account balances and the appreciation of real exchange rates can be taken as the leading indicators of currency crisis (Kaminsky & Reinhart 1998:7). Interest rates are often not market-determined in LDCs and may be politically administered. While in some cases high interest rates are favored in order to benefit the unproductive *rentier class* which lives on interest earnings, in others, a regime of low interest rates may be invoked to favor the capitalist class for borrowing from banks. But the tragedy is that very often interest rate manipulation does not serve the purpose for which it is designed. Kindleberger seems to be right in saying that a high interest rate may attract funds or repel them depending on the expectations that a rise in interest rate generates (Kindleberger 1996:8).

The emphasis on heavy industries, in pursuance with the Soviet model of industrialization, and in sympathy with the philosophy of import substitution, led to the genesis of government failures in many developing countries. Government intervention sometimes leads to unpredictable and undesirable consequences. For example, an attempt to introduce rent controls often leads to reduced supply of houses. Very often, the ends of government policy are not sufficiently clear and there arises an end-means conflict. The trade-off between the conflicting macro objectives is not determined on the basis of society's

preferences but by personal motives and political agenda or, there may be entirely unwanted trade-off points. Also, there may be implementation failures due to a number of reasons including corrupt practices, favoritism, nepotism and so forth. Moreover, government intervention in many cases is very expensive, and the resultant net benefit may be much less than the cost involved. In fact, the precise relationship between the instrumental variable and the policy variable may not be known to the government before policy formulation. In such a situation, there is either over-shooting or under-shooting. Under these circumstances, the introduction of government to mitigate market failure generally leads to the substitution of one type of inefficiency for another. The uncertainty that arises in the matter of macro policy-making during the twilight period of market and government failure is basically motivated not so much to justify the growth of the economy as to gain political mileage

### **Politics of Privatization**

There were wide-spread government failures in the 1960s and early 1970s in many developing countries. In the vortex of the changing macroeconomic scenario, many LDCs were compelled to revise their development strategies by introducing a number of quasi-market reforms that included export promotion measures, liberalization and privatization. But the privatization plan was opposed in those countries where bureaucracy was strong. Such countries included Singapore initially and the countries in South Asia, including India and Bangladesh. In many of these countries, privatization efforts are still piecemeal. However, some countries of East Asia did benefit from liberalization and privatization. But privatization was not free from politics. Through privatization, the government wanted to relieve itself of some of the macroeconomic public responsibility

that it was originally endowed with, and in some cases, it developed a system of *crony capitalism* where the benefits of privatization were largely shared by the cronies of the ruling political elites.

Privatization is essentially a political decision, and as such, political factors have remained overwhelmingly more decisive than any other factor. A study of privatization in the ASEAN countries shows that, generally, politicians are in favor of privatization because they can potentially reap some gains out of the privatization bargain. They are also able to endow some benefits and advantages to their close relatives, family friends and cronies. The cronies gain in buying the shares of privatized industries at a lower rate and selling at a premium in future. As a matter of fact, *underpricing of shares* to be sold in the market has remained an important mechanism to benefit the cronies at the cost of huge losses to the state exchequer. The government often wants to reduce its financial burden, and shirk social responsibilities of providing public goods.

However, at times, the government may not be interested in privatization because it finds that, by so doing, it will lose its monetary benefits, power and control. Thus, the privatization attempts of Philippines Airlines and the Manila Hotel was not a success because the cronies of President Aquino were not ready to surrender the advantages they were deriving from the control of these organizations (Milne 1991:328). In the Philippines, nepotism, favoritism, and corruption stood in the way of privatization of public enterprises. The pork-barrel politics of survival during the Aquino regime was responsible for the negative political will for privatization. In India, privatization is often opposed by trade unions which are afraid that it would lead to job losses. Bureaucrats there opposed it because they were afraid that it would minimize their



rent-seeking power and workers opposed it because it would bring about a new work culture based on reward for hard work.

When a government does not want privatization of a particular public enterprise, it offers the excuse of *national interest* and/or *strategic issues* involved. This happened in the cases of the non-privatization of the Philippine National Oil Corporation, and many state enterprises of Indonesia in 1989. In Indonesia, the privatization process is often stalled by the government because the prospective buyers were the less-wanted or unwanted rich Chinese business people.

A pressure group which has an important direct role to play in the privatization process is bureaucracy (and top managerial personnel). In general, bureaucrats are not interested in losing their empires and control over public enterprises, which have traditionally remained their citadel of power, prestige and patronage. These enterprises are valuable sources of *rent-seeking* activities. Bureaucratic resistance has been primarily responsible for delays in privatization in Thailand, Indonesia, Philippines and India. In the case of Singapore, the bureaucrats who were on Boards of government enterprises had disapproved of privatization in the first instance. In Malaysia too, bureaucracy in general did not have much commitment to privatization. In Singapore and Malaysia governments being very strong, and bureaucrats lost the power war with ministers and politicians. In Malaysia, in particular, bureaucracy is too weak to go against the government on any issue whatsoever. Thus, it had to support the privatization process from the outset.

From the foregoing, it becomes clear that the whole process and speed of privatization in ASEAN countries has been influenced by interactions of a system of *political duopoly*, where government (including politicians and ministers) and bureaucrats are the two main

players. The duopoly may be collusive or non-collusive in nature. When both players agree or disagree jointly to privatization, the duopoly becomes collusive. But when their interests are diametrically opposed the duopoly becomes non-collusive. As a matter of fact, the nature of political duopoly has its bearing on the tempo of privatization (Ghosh, 2000a).

Through privatization, FDI and liberalization, the East Asian economies in general could manage to increase the rate of economic growth to a significant extent but would not be able to sustain their economic windfalls beyond a decade or so. The financial crisis of 1997 amply proved that a market has its own limitations and cannot be expected to automatically adjust to changing circumstances: the invisible hands do not always bring about the desired equilibrium. The Asian financial crisis can be explained by political economy factors. During the course of industrialization in these countries, commercial banks were given a predominant role. These banks were the instruments of industrial development in much the same way as in the Schumpeterian model. They were also the institutions through which state capitalism and crony capitalism found their full expression. These banks enjoyed implicit, and in some cases even explicit, guarantees from the ruling party. This gave them an absolute empowerment for both borrowing from abroad and lending to domestic investors. Since banks are government-sponsored institutions, they lent out huge amounts of money to political cronies even without necessary collaterals, and thus violated the basic principles of commercial lending. The implicit government guarantees acted as a moral hazard both for short-term borrowing by banks from abroad, and for the international institutions to lend out money to these banks. This opened a *Pandora's Box* in relation to the problems of non-performing

loans, mounting short-term debt and the vulnerability of the banking system. When the government guarantees foreign liabilities of the banking system, it creates an additional claim against the thinly spread forex reserve. Thus, in a sense, the banking crisis that was precipitated by political action could really provoke a financial crisis as in the case of the East Asian economies (Ghosh 2000).

Over the years, in many developing countries of Asia and Latin America, a few such symptoms became tell-tale signs of which included high rate of growth of inflation, pronounced fiscal deficits, growing unemployment, increasing balance of payment deficits and gradual export slowdown. However, the prevalence of weak macroeconomic fundamentals gradually contributed substantially to depreciate exchange rates.

### **Political Instability, Exchange Rate Depreciation and Inflation**

Taking a cue from the Mundell-Fleming model, one can state that for an open economy with political instability, the actual interest rate is determined by a risk premium which can be looked upon as a compensation for political uncertainty. If government policy raises the risk premium, there would be capital inflow and subsequently, a lower nominal exchange rate but no increase in the level of income (Mankiw 2003:329). The policy decision to counteract the falling tendency of the domestic exchange rate, if at all, is also a political matter. The fact that political instability is an important determinant of a country's risk premium and hence the accompanying high interest regime is borne out by the experience of Mexico in 1994 and the crisis-ridden East Asian economies of 1997. In all these cases, domestic interest rate rose appreciably despite heavy capital inflow, defying the basic tenets of the Mundell-Fleming model, and the

nominal exchange rate depreciated simultaneously. All these factors sped up the process of the onset of a currency crisis.

Political instability however, is a function of many different types of factors and forces, such as, frequent changes in governments, in policies, in power relations and in future expectations about political twists and turns. Political instability can be measured by the actual frequency of transfer of political power. Political instability has been found to be positively associated with inflation, and it also sustains inflationary expectations which may be incorporated in wage bargains. Since political instability also aggravates inflation, which in turn escalates inequality, there seems to be a relationship between political instability and income inequality (see Albanesi 2001). Income inequality may also have a positive impact on political instability.

Political instability, income inequality and economic growth are mutually correlated. Venieris and Gupta (1986) find that political instability has a negative impact on savings. Political instability can thus reduce investment and growth. An empirical study by Ben-Habib and Spiegel (1992) indicates that socio-political instability reduces the incentive for investment. Poor countries are generally more unstable because they are not rich, and they are not rich because they are not politically stable (Alesina and Perotti 1994:359). Politically unstable poor countries thus have a vicious circle of poverty and instability.

A high degree of income inequality is often associated with illegal activities, social instability and unrest. In a society with a significant degree of income inequality, the majority of voters will vote for higher taxation on the richer classes for many obvious reasons, and this apparently discourages both investment and growth. The model presented by Alesina and Rodrik (1994) concludes that there is an inverse

relation between income inequality and growth. Higher income inequality leads to higher taxation and more government expenditures on pro-poor programs. Income inequality is thus an important determinant of socio-political instability, which produces adverse effects on economic growth.

### **Concluding Observations**

One of the essential tenets of the new political economy—that nothing should be left to the discretion of the government because it cannot do anything right—does not seem to be correct in light of the empirical experience of many countries in both the developing and developed world. Discretion can reduce the rate of inflation, as the evidence of central bank independence shows in a number of cases, and it is indeed possible to have a free lunch which (is usually undreamt of by economists). If macroeconomic policy-making can be made free from pernicious political influences, an economy can perhaps get rid of political business cycles, if they are at all present.

But election politics is often accompanied by heavy fiscal deficits. In modern states, deficit bias is often associated with the nature, character, durability and the expenditure policy of the government. In general, coalition, democratic and unstable governments are highly deficit-prone. The question of political stability is, after all, a critical issue. The market system that generated political (and hence economic) instability in many developing countries at the initial stage of their industrialization process led many to believe that there was market failure in such countries. Thus, for bringing about development with stability, the state was given a clean mandate. But the state became an instrument in the hands of many power groups. Policies became more partisan and politically motivated, and the opposing interests of the power groups delayed the

process of macroeconomic policy-making and its implementation. Excessive monetary-fiscal expansion led to economic-financial instability and in many countries, the symptoms of both market and government failures became all too apparent.

In the event of government failure, some quasi-market reforms including liberalization and privatization were introduced in many developing countries. But such reforms were also not free from political moorings. Whereas in some countries, privatization generated and expanded crony capitalism, in others, it did not make much headway as there were group pressures and opposition against privatization. But in spite of privatization in East Asia, the growth of crony capitalism and macroeconomic vulnerability played a major role in generating bank failures, financial instability and the depreciation of exchange rates.

In fact, political instability is highly correlated with a number of macro variables including inflation, income inequality, fiscal deficits and exchange rate depreciation. A higher degree of political instability increases the risk premium of a country which leads to higher domestic interest rates, less investment and so forth, so as to give rise to exchange rate depreciation with all the attending pessimism that makes a country macroeconomically weak and vulnerable. In the present-day world, political instability arises out of, and is often exacerbated by, not only frequent changes in the government and its policy, but also by the influence of pressure groups, uncertainties and externalities both from within and without. And in every situation, the state has to struggle hard to remain in power and to achieve its short-run objectives. Thus, it is obvious that macroeconomic policy becomes a reflection of the temper of the political will and preference at a particular point in time,

and no macroeconomic policy is indeed neutral in its formulation and implementation.

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## Privatisation

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### **Defining Privatisation**

Despite common usage, the term privatisation refers more to a family of meanings rather than one specific technique. To the reformer, it symbolizes a new way of looking at society's needs and re-thinking the role of government in fulfilling them, as Savas (1987) put it. A movement with political origins and objectives, privatisation essentially means reducing the role of government and increasing the role of the private sector (Starr 1989:22). The most common use of the term privatisation relates to the sale or partial sale of public enterprises—denationalisation, but there is a wide range of activities that have been seen as privatisation around the globe. Peter Drucker has been attributed with coining the term in the late 1960s when he observed that whilst governments were good at making difficult decisions, they were poor managers – and that consequently, the private sector ought to be more involved in the daily work of government. Not surprisingly, the second most common use of the term privatisation relates to contracting-out the provision of public services to the private sector (Hodge 2000). This category encompasses service contracts, franchising, distributing vouchers to private consumers, or the subsidization of public services. Other uses also include load shedding, in which the state withdraws from service provision, deregulating monopoly powers so that competition is encouraged or private substitution occurs, as well as the introduction of user-pays philosophies.

Recent use of the privatisation label mostly refers nowadays to four areas; the sale of enterprises as made famous through Prime Minister Margaret Thatcher's sales program in the United Kingdom (UK), the contracting-out of government services, the use of 'public-

private partnerships' (PPPs) and the adoption in developing countries of the philosophy of 'private sector development strategy' (PSDS) in order to develop and strengthen the national market economy. What is clear from these definitions is that the global use of the terminology is often loose and can cover a range of government reforms relating to ownership change and contracting strategies as well as dimensions including competition, regulation and accountability.

### **History**

The search for what ought be regarded as public and what ought be private has been central to political philosophy for a thousand years. The public-private divide has a long pedigree. It is little wonder that strong debate occurs over proposed privatisation policy reforms. Some early examples of the use of private sector resources to meet government policy objectives are well known and include Mathew the tax collector in the bible and the employment of (private) mercenaries to fight wars on behalf of national governments. Other examples are less well known, but nonetheless show clearly that government has always had a robust relationship with the private sector through history. Illustrations include the cleaning of streets in 18th century England, the building of the British railways in the 19<sup>th</sup> century or the earlier workings of the United Kingdom Treasury which, centuries ago, was effectively a group of private accountants, and the operation of the 'privateers who were largely responsible for the spread of the British Empire. Indeed, some 83 percent of the 173 ships that conquered the Spanish Armada in 1588 under Sir Francis Drake were contractors to the Admiralty. All of these examples attest to the fact that private resources have always played a large part in government. But whilst the success and strength of these arrangements

were not in doubt, probity often was (Wettenhall 2005).

Perhaps a more central thread to the present-day privatisation debate concerns the history of State Owned Enterprise around the globe. Traditionally the provision of essential services such as electricity, gas, post, and telecommunications marked the deliberate use of government power in the face of both market and private sector failures as citizens demanded the provision of essential services across nations. Indeed, governments around the globe throughout the twentieth century saw state owned enterprise as a development stimulator as well as a provider of services and infrastructure (Wettenhall 1965). Often supported by powerful and effective managerial leaders – such as Robert Moses who oversaw massive developments in New York's transport infrastructure between 1924 to 1963; Sir John Monash, who in the 1920s oversaw the creation of electricity supply systems across Victoria, Australia; and others around the world – the public enterprise era often saw the frequent application of great innovation and creativity (see Russell 1990). The institutional models adopted by governments varied along a continuum. At one end was the traditional, simple government department under the direct control of a relevant Minister. At the other was the more sophisticated and politically independent model of the statutory corporation. Here, the organisation was subject to the laws and financial disciplines of the corporation, but, although publicly owned, was not under the direct day to day control of a Minister. Other possibilities also existed in terms of Boards, Trusts, Committees and 'Qangos' (Quasi-Autonomous Non-Government Organisations) (Wettenhall 1965, Russell 1990).

This continuum evolved into a line of logical philosophical progression for State

Owned Enterprises from state ownership and control to privatised operation. The driving philosophy was that greater independence promoted commercial viability and the benefits and costs of using private enterprise for public works in comparison to a public labour force were often strongly debated through a 'well rehearsed argument' (McIntosh et al. 1997:39). The broader privatisation debate, seen as a war by some (Hodge 2002), became a battle on at least three fronts; a philosophical battle between individualism in preference to collectivism; a public policy battle of implementation (with service delivery increasingly being preferred through private rather than public mechanisms); and struggle of capital interests against both human and social interests. Through most of the twentieth century, the United Kingdom swung away from private ownership towards nationalisation of 'the commanding heights' of the economy, and then swung convincingly back to private ownership in the subsequent two decades.

### **Theories Underpinning Privatisation**

Several conceptual bases exist for the modern trend towards privatisation (Hodge 2000). The most often voiced theories fall in the arena of economics, with increased economic efficiency as the means of increasing the well being of citizens. Intellectual foundations here include Public Choice Theory, Agency Theory, and Transaction Cost Analysis as well as Property Rights Theory and Governance Structures (Boston 1991, Spicer et al 1991). To these economic ideas we might add a few other influential reform concepts such as measurement issues and the notion of managerialism or new public management. Each of these concepts directly appeals to our rational desire for efficiency improvements through better organisational performance and control. The central underlying belief is that self interest

dominates human behaviour (Self 1994; Stretton and Orchard 1994). Selfish economic interests thus provide the primary motivation and lubricant of human behaviour, and individuals are rational utility maximisers who can express their personal preferences more efficiently through market exchanges than via political participation (Self 1994, Stretton & Orchard 1994). These public choice ideas reject concepts like public service, the 'public interest' or even 'social justice' (Boston 1991). The implication here is that the role of the state should be reduced because bureaucrats look after their own interest not the public interest and that functions such as regulation, policy advice, and the delivery of services should be undertaken separately. Moreover, governments ought to 'steer not row' (Osborne & Gaebler 1993) and service delivery should, where possible, be privatised through either contracting out or divestiture.

Several criticisms of these ideas exist. Firstly, the behavioural assumption of 'homo-economicus' is seriously flawed. People are as generous, altruistic and accepting of obligations to others as they are selfish, they are clearly co-operative as well as competitive, and are swayed by beliefs about which party will do the most for national prosperity and welfare as their own pocket. Boston (1991:13) put it nicely arguing that human beings are not merely economic beings, but also political, cultural and moral beings ... with attitudes, habits, beliefs, aspirations, ideals, and ethical standards. Any theory which ignores these contextual factors is 'at best incomplete, and at worst misleading and damaging'. Second, public choice theory suffers from a lack of empirical validation (Boston 1991). As well, Self (1994) argues that the notion that governments which minimise their responsibilities will therefore be more impartial between groups and interests is

quite wrong. Nineteenth century governments were small, but were also strongly biased towards the interests of property and capital until more balanced political and social voices forced improvements to the appalling working and living conditions of citizens. These public choice ideas must therefore be regarded as limited models at best. Likewise, the foundational ideas can be questioned for agency theory. Agency theory recognizes that the owners of a company are not the managers, and that—because their interests may diverge—some monitoring is necessary for control purposes). Transaction cost analysis recognized that firms aim to minimize the costs of transacting their business by vertical integration or by taking over firms to whom they sell or else their suppliers. And property rights theory assumes that the more individuals stand to gain from tending to their property, the better it will be tended.

Each of these theories have been subject to critiques, such as those of Boston (1991) and Spicer et al (1991). We should also reflect on the degree to which many of these privatisation theories seem to be remarkably loud on the positive human traits (of better meeting performance objectives with financial incentives for instance) whilst being silent on the negative traits (such as the increasing tendency for financial incentives to encourage fraud, an Enron-like lack of accountability, and perverse social incentives.)

Added to these ideas is also the plausible idea that privatisation does not have an economic rationale at all, but is merely a political mechanism aiming to facilitate the achievement of non-economic goals such as sell-offs requested by bodies such as the World Bank, privatising to increase business confidence or act on consultant advice, privatising to encourage less corruption than in public enterprise, the redistribution of power away from unions or privatising under



an ideology believing, for instance, that good government is small government (Hodge 2000). Indeed, the largest driving forces underpinning moves towards greater use of private resources may have been borne in politics rather than economics. Guttman and Willner (1976) noted the early existence of what he called a shadow government of contractors in the US through the 1970s, and more recently coined the term 'Shadow Pentagon' in the context of the recent Iraq war, labeled by some as one of the globe's biggest public-private partnerships of the modern era (Hodge 2004a). The greater use of private contractors seems to have been a consequence of three factors; the continual rise in the demands put on governments in terms of legislated services for citizens, the ongoing political rewards for reducing the overall size of government as a whole in terms of personnel numbers (despite continuing to promise more and better services) and the change from a 'government' model to a 'governance' model that values networks and other linkages between the public and private sectors. Outsourcing under this view has essentially become inevitable (Hodge & Martin 2005).

### **Privatisation Patterns and Trends**

With tens of thousands of privatisations occurring around the globe, an article such as this cannot cover individual jurisdictions. Nonetheless, some highlights and examples are appropriate. The OECD lists the UK, New Zealand and Australia as the biggest privatising countries in the world through the 1990s on the basis of divestiture revenues earned as a proportion of gross domestic product (GDP). These proportions were around 1.8 percent (New Zealand), 1.7 percent (Australia) and 0.7 percent (UK), respectively. On the basis of gross divestiture revenues, the list featured the UK (at around \$US62 billion), Australia (\$US45 billion) and

Italy (\$US40 billion) (Reserve Bank of Australia (RBA) 1997). In terms of developing economies the biggest privatisers on the basis of GDP proportions were Argentina (9.9 percent), Peru (8.6 percent) and Malaysia (8.5 percent) (Cook and Uchida 2003). And on the basis of gross revenues from enterprise sales the top billers for developing countries were Brazil (\$US34.6 billion), Mexico (\$US33.4 billion) and Argentina (\$US27.9 billion). Around \$US850 billion was raised worldwide from the divestiture of state-owned enterprises alone throughout the 1990s.

The most widely known privatisation program of course was that of Margaret Thatcher who essentially led the charge. In doing so, she overcame the hesitation that huge amounts of private capital could be raised without any market consequences such as 'crowding-out' of capital from other areas of industry. Her divestiture program also gave the warm assurances of political feasibility and attractiveness in terms of strong leadership to the business sector and acceptance by citizens. Details of the UK divestiture program are well covered elsewhere (Bishop et al 1994, Parker 2004). Nearly all state owned enterprises (SOE's) trading in the competitive sector were sold and later utilities such as water were also sold (RBA 1997). Elsewhere in the European Union (EU), governments were also privatising, with receipts varying between \$US15.6 billion to \$US67.5 billion each year through the decade during the 1990s.

In New Zealand, a bold experiment was taken by a labour government as it launched into wholesale privatisations in 1987 in a bid to overcome a public debt (of 32 percent of GDP), a sliding credit rating and living standard in world terms, and a crisis of confidence in the midst of a huge currency devaluation in the NZ dollar; Mascarenhas (1991) and DeVries et al. (1998). Australia's

federal system of politics also saw the federal Howard liberal/national coalition as well as some state governments (such as the Kennett liberal/national party coalition government in Victoria), delivering privatisation policies with enthusiasm. Sales amounted to some \$A96.6 billion, and, equally spread between federal and state-levels, covered traditional utility services such as electricity and gas, as well as transport, communications and financial services (Hodge 2003). A huge range of business types were divested, mostly through trade sales, with various political justifications, and proceeds were mostly used to reduce public sector debt. In terms of contracting-out services, most Australian governments also contracted out services in a wholesale manner. Many state governments have also recently been entering into long-term PPP business relationships with private partners, modelled largely on the United Kingdom's Private Finance Initiative (PFI) policy.

As well, developing countries probably contributed around 30 percent of global divestiture revenues last decade (Cook and Kirkpatrick 2003). This was mostly from the sale of infrastructure assets such as telecommunications and power. Latin America accounted for the largest share of non-OECD privatisations, although central and eastern Europe and central Asia sold the largest number of enterprises.

### **Privatisation Objectives**

There has been a huge, though not widely acknowledged, diversity of objectives for privatisations around the globe. Hodge (2000) lists 76 explicit and implicit goals documented in the privatisation literature. The best known and most commonly quoted objectives for the divestiture of government enterprises relate to economic efficiency. But this was not the original reason for Thatcher's early divestitures. As Whitfield (1992) put it,

divestitures originated as a political and financial strategy, and although privatisations in the UK followed the general aim of increased industrial efficiency, 'the economic rationale was appended later'. The biggest early driver appeared to be winning the battle with the British unions, who had previously held the country to ransom during their 'winter of discontent' in 1978 as well as the need for cash into government coffers. Having said this, there is also no doubt that since the early Thatcher years, the common espoused aim of privatisation programs world wide has had a central theme of improved economic efficiency. Other objectives of enterprise sales have included funding autonomy (or access to capital), fiscal management (including revenue raising and public sector debt reduction), benefits to the consumer (such as better services, reduced prices or more choice), and population share ownership. As well, the objectives of privatisation have, on occasions, been seen as more sophisticated. For instance, Parker (2003) suggests that in the case of the European Union, as well as efficiency and debt reduction goals, two further objectives have dominated. Privatisation was firstly seen as being able to make a contribution to developing domestic capital markets. As well, it was seen as a necessary response to measures within the EU aimed at liberalizing markets. If privatisation is seen in the narrower vein of contracting-out services, the objectives of government have almost universally related to economic efficiency and cost savings (Hodge 2000), as well as limiting the size of government in terms of personnel numbers (Guttman 2003). More recently, contracting-out goals have also included saving scarce management time, obtaining expertise, and retaining flexibility as well. The most recent chapter to the privatisation story is that of public-private partnerships. These likewise promise better efficiency and strengthened accountability as well as appearing to inspire

business confidence. Launched with an air of improving the financial capacity of government to provide public infrastructure, PPPs also claim superior delivery of projects on-time and to-budget compared to traditional procurement methods. Of course at the broadest level of private sector development strategy (PSDS) in developing countries, the objectives of privatisation as a strategy framework for development relate to strengthening the economic engine powering a country. Aimed essentially at broader development needs, activities undertaken under the PSDS banner might seek to strengthen the rule of law, reduce corruption and weaken bureaucracy as well as complete privatisation activities such as divestitures and contracting-out government services.

As well as the explicit objectives of privatisation, we could define several differences between the values inherent within a collective or public sector orientation and those of a private or market sector model (Pollitt 1993). On the one side, the political (or public sector) model sees collective choices being made through the mechanism of citizen voices in the polity, whilst, on the other, the market model sees individual customers as sovereign and with competition as the operating mechanism. There is a search for justice on the public side, and a search for market satisfaction and individual wealth on the private side. There is a contrast between the notion of equity within market transactions and commercial decisions behind closed doors in the case of the private sector, and the equity of need and the desire for openness for public action in the case of the public sector. The pressure for change is seen in the private sector to be exit through the buying decision, compared to voice as a pressure for change in the public arena.

Having said all this, the objectives of privatisation over the past few decades have often not been expressed clearly but have

been buried, implicit, conflicting and subject to as much spin, color and policy salesmanship as might be expected of any other government policy initiative.

### *Politics*

There have been several distinct political characteristics associated with privatisation activities over the past few decades. First, the biggest drivers of privatisation have usually been overwhelmingly pragmatic rather than decisions based along traditional ideological lines. This pragmatism has included for instance the need to bust union power, the simple need for cash or in the case of developing nations, the strict conditions attached by the World Bank/International Monetary Fund (IMF) prior to the release of badly needed loans. These needs seem to have transcended all sides of the political spectrum with privatisations now having been undertaken by governments including traditional conservative governments, labor governments and radical conservative governments.

Second, powerful, simple and appealing messages such as 'steering not rowing' (Osborne & Gaebler 1993) and sticking to 'core business' have been sold by the consulting sector and have underpinned privatisation activities. This is despite the strong intellectual critiques of the reinvention movement and of the concept of 'core business' by commentators such as Fox (1996), Kettl (1993) and Mulgan (1998). Such phrases have assisted in making privatisation policies an easily digestible and comfortably sold policy platform.

Third, the popularity of privatisation activities such as divestitures with the capital markets has also ensured the rise of privatisation. The steady rise of citizens as shareholders as well as the tendency for voters to be concerned with economic growth as a priority voting matter would no doubt

have encouraged greater voter confidence as well.

Fourth, within the context of developing countries the IMF has encouraged privatisation, ostensibly under the guise of economic policy. But as Stiglitz (2002) says the very notion that one could separate economics from politics was itself naive and narrow, and its lending conditions clearly went beyond economics and were essentially political. The ironic result has been that, viewed as a front for US colonial capitalist interests, 'the IMF is vilified almost everywhere in the developing world'.

So, have the bold political promises made for privatisation been achieved? This is the subject of the next section.

### **Assessing the Effectiveness of Privatisation**

The 'success' of privatisation is hotly contested. With the huge range of objectives being sought by governments, it is little wonder. It is a politically charged question. But our assessment also turns on the type of privatisation activity undertaken and on the sophistication with which these activities have been undertaken in different jurisdictions. Not surprisingly, conclusions have been mixed.

#### *Enterprise Sales*

Several authors have reviewed the global success of divestitures including, for instance, Hodge (2000), Martin and Parker (1997), Parker (2004), Megginson et al (1994), Boubakri and Cosset (1998), D'Souza and Megginson (1999) and Cook and Kirkpatrick (2003). Most authors acknowledge the cash gains to governments and labour productivity gains in divestitures, but many authors from this list have also been surprised at the modesty of the gains observed, and the limited service improvements for citizens. For example, Hodge (1997, 2000) looked at 230 evaluation reports and 10 468 before and after measurements of performance in a meta-

analysis of global divestiture results. Modest gains were confirmed for the financial performance of privatised firms (i.e. return on equity and return on sales) and productivity, finding slight improvements on average. In both cases, only a small part of the gains measured were associated with the enterprise sale itself, however, as performance improvements also occurred in organisations which were not privatised. Better capital investment was detected following privatisation, but no simple direct link between the size of the private sector and economic growth was found. Likewise, parallel comprehensive investigations by Martin and Parker (1997:215) also found 'little evidence of any systematic improvement in performance', observing performance improvements in 82 instances (51.6 percent) and deteriorations in 77 instances (48.4 percent).

Divestitures have usually seen strong winners and losers, too. The World Bank's own 1994 report on projected benefits from divestiture privatisations in the UK, Mexico, Malaysia and Chile, for instance, found investors winning in eleven of the dozen cases analyzed, whilst citizens either gained nothing or lost in two thirds of these (Galal, et al 1994). The statistical confirmation of significant shareholder returns with privatisation contrasts the broken rhetorical political promises made to citizens and consumers of lower prices and higher quality services (Hodge 2000). Individual case studies illustrating this point include the sale of Argentina's telecommunications company ENTEL, where divestiture resulted in Argentina as a country losing some \$US2.2 billion, despite a 'world-wide welfare gain' being calculated because of massive offsetting gains made by New York Stock Exchange investors (Abdala 1992). Likewise, Ralston Saul (1997) reports that the privatisation of 80 percent of Mexico's state

firms created 30 billionaires, all friends of the president or the party in power, whilst real wages plunged 52 percent. At the extreme, citizens of Cochabamba, Bolivia, rioted in the streets after the price of water tripled under a World Bank privatisation project. This was only stopped after the privatisation legislation was repealed and civilians took over water arrangements (The Corporation 2003). Deepening inequality appears unfortunately to have been a worldwide theme with divestitures.

Specific lessons from divestitures in different jurisdictions have differed. Parker (2004) listed 17 analyses of the UK experience and noted that the program of 51 divestitures was an important cultural, economic and political core to Thatcher's desire to reverse the 'corrupting effects of socialism' (Thatcher 1993). Large labour savings were achieved (with British Rail for instance personnel numbers reducing from 238 000 at privatisation to 125 000 in 1999) and prices declined in real terms (by around 26-34 percent) over the 1990s although industry gained bigger reductions than poorer consumers. The overall theme then was one of a continued pattern of historical improvements gained prior to divestitures, with the modest improvements essentially being due to better competition and stronger regulation of new arrangements rather than the changes in ownership per se. To Parker's mind, nevertheless, privatisation helped to create a more conducive environment for private investment compared to previously, less efficient, public enterprises. These modest improvements contrasted the large political promises made in terms of major benefits promised to citizens. For the case of Australia, Hodge (2003) concluded that privatisation reforms had been both a political and economic success, though again, benefits to consumers appeared to be modest, and strong

independent regulatory frameworks had been needed to achieve consumer benefits.

Experience in developing countries has been tracked by Cook and Kirkpatrick (1988, 1995, 1998) and has been one fraught with complexity and diversity. Cook and Kirkpatrick (2003), Boubakri and Cosset (1998) all likewise present surveys of divestiture assessments in developing countries and show the sobering experience to date. Overall, Cook and Kirkpatrick (2003) found limited evidence of success following privatisation at the macro-economic level and for issues of social impacts, but stronger evidence of success at the level of the firm with 80 percent of firms increasing efficiency and 63 percent of firms improving profitability. Numerous jurisdictions might provide individual examples of divestiture learnings. One of the starkest has unfortunately been that of the former Union of Soviet Socialist Republics, where poor advice was provided by the IMF to privatise quickly at all costs. Fraudulent and corrupt activities were then free to occur in a vacuum of effective state governance and whilst many divestitures occurred, they were highly ineffective and made everyday conditions for most Russians worse not better (Stiglitz 2002). These days, some 70-80 percent of organisations are reputed to have to make corrupt payments to the mafia (Prokopenko 1998).

### *Contracting-Out*

Meta-analytic research has summarized 23 914 available global measurements before and after contracting-out government services from 129 evaluation reports (Hodge 2000). Contracting-out seems to have worked well in some areas and not in others. On average, a significant cost saving of around 6 percent was found for contracting public sector services, although the bulk of the evidence related to strong savings in the areas of garbage collection, cleaning and maintenance

services (i.e. between 19-30 percent savings), rather than the lack of savings found for other services (which varied between an 8 percent saving to a 24 percent cost increase). Thus, different services experienced different success. In terms of service quality, the little empirical evidence available indicated that service quality was unaffected, on average, by contracting. Sometimes it was better, sometimes not. Importantly, contracting *either* in-house or outside the organisation both led to cost savings, suggesting that service specification and competition raised efficiency, not the sector doing the work. Unfortunate social impacts appear to have occurred with contracting reforms, with women and minority groups bearing the brunt of contracting efficiencies internationally. The potential for businesses to exert undue influence over political decisions, for contracting to be subject to corrupt practices or else lack transparency due to ‘commercial-in-confidence’ claims, were all seen to be real risks as well.

### *PPPs*

The PPP notion has a wide range of meanings around the globe, although the UK Private Finance Initiative (PFI) has become a centre-piece of renewed privatisation activity to some governments (Osborne 2001; Hodge and Greve 2005). Whilst a long term partnership philosophy is not strictly new, some aspects of modern day PFI type PPPs are new. These include the preferential use of private finance arrangements, the use of highly complex contracts to provide the infrastructure or services, and the altered governance and accountability assumptions accompanying this (Hodge 2004b).

Solid evidence on such PPPs is limited, and controversial. The early UK Treasury Task Force reports of Arthur Anderson and LSE Enterprise (2000) and National Audit Office (2000) remain the most widely quoted

sources. The first of these looked at 29 business cases from departments and estimated cost savings of 17 percent compared with the projected costs under public provision, whilst the second report analysed seven specific PFI projects and found cost savings of 10-20 percent. In both instances, savings in these business cases were due mainly to the calculus of risk transfers assumed from the public to the private sector. The more recent analysis of Pollitt (2002) also resulted in a careful pass mark, and suggested that PFIs were ‘successful for prisons and roads but of limited value to date in hospitals and school projects’. Indeed, in a sample of ten major PFI case evaluations undertaken by the UK National Audit Office (NAO), the best deal was probably obtained in every case, and good value for money was probably achieved in eight of the ten cases. Also supporting the PPP case is the reality that traditional public sector infrastructure project delivery has hardly been a model of efficiency itself. It has been one characterized by ‘a history of completing investment projects over budget and late’ according to a study by the Department of Transport (2002) in which some 250 London Underground projects between 1997 to 2000 experienced cost overruns averaging 20 percent. Furthermore, support comes from the NAO (2001) in the UK, which indicated that some 81 percent of authorities viewed the value-for-money from PFI projects let prior to 2000 positively; and from Mott-Macdonald (2002) and the NAO (2003), both of which reported PPPs as being delivered on time more often than traditional infrastructure provision arrangements. Outside the UK, Bloomfield, Westerling and Carey (1998) saw PPP lease purchasing financing arrangements in the United States as ‘wasteful and risky’ whilst Walker and Walker (2000) likewise saw Australian PPPs as ‘misleading accounting trickery’. In

Europe, Greve (2003) even characterized the Farum PPP case study as ‘the most spectacular scandal in the history of Danish Public Administration’. As well, the assessment of eight Australian case studies by Fitzgerald (2004) concluded that evaluation results depended on the discount rate adopted in the assessment. Using the current 8.65 percent discount rate for public sector comparator calculations led to the conclusion that a 9 percent cost saving was being achieved against traditional methods, whereas the use of a of 5.7 percent discount rate led to the opposite conclusion—that PPP arrangements had led to an estimated 6 percent greater cost and the likelihood that the \$A2700 million presently being repaid by the Victorian government was around \$A350 million higher than it should be.

### *PSDS*

Private Sector Development strategy recognises that a dynamic private sector is crucial to long term economic growth and poverty reduction. It also argues that the single most important route out of poverty is finding a job and observes that in, say, Venezuela over 1997-98, some 89 percent of people who were lifted out of poverty did so through getting a private sector job (International Finance Corporation 2000). Contrary to much of the pro-public sector rhetoric, it furthermore acknowledges that in developing countries, state owned utilities have effectively not delivered essential services to the most needy ahead of the middle class. Wallich (2001), for instance, argues that ‘public infrastructure monopolies have largely failed the poor’ and quotes the price of water being purchased from informal vendors as twenty times higher than the price of piped water, and the cost of grid supplied power as ten times that of paraffin in kerosene lamps. The private sector certainly plays an increasingly strong role in

developing economies - probably stronger than that of PSDS activities of the development agencies - with the consequence that the evolution of an ‘enabling environment’ will continue to be a huge challenge. Such strategies, ought to be ‘about a good balance between the complementary functions of the state and the private sector’ rather than about indiscriminate privatisation per se (World Bank 2002:i). Clearly, the complexity of development economics and cultural change make reliable assessments very difficult here.

### **Regulation, Accountability and Transparency within Privatised States**

A central lesson from the early UK privatisation program, as well as subsequent global experience of divestitures, has been the need for more attention to the dimensions of regulation and competition. Rather than the state reducing its role in the economy, citizens have demanded strong professional and independent regulatory frameworks to ensure that privatised markets for services are well governed. Thus, despite the rhetoric of ‘de-regulation’, the reality for successful privatisations has been ‘re-regulation’. The establishment of Offices for water, electricity, gas and telecommunications ombudsmen or Regulators General all exemplify this trend. This notion of powerful independent regulators being central to governing structure appropriate for the privatised state has spread quickly around the globe, and according to Gilardi et al (2006), numbers have expanded some seven-fold since the late 1980s.

In terms of accountability, many authors argue quite simply that accountability increased through enterprise divestitures and outsourcing contracts. It is true that divestitures create distinct enterprises with clearly defined lines of responsibility instead of public sector enterprises being submerged

in the depths of government ministries (Bishop et al 1994). It is also true that instead of work being undertaken internally, service requirements are specified carefully through a legal contract when services are contracted-out of government. These views are simple and have some truth, at least in terms of narrow financial reporting and managerial requirements. But accountability in the context of essential services in a liberal democracy is a more sophisticated and contested notion than financial returns to shareholders. Accountability in today's state might be better viewed as a series of complex accountability 'networks' (Hodge 2005). Overarching networks of political accountabilities for parliament and the government operate at the highest level, and are underpinned by other networks of administrative, managerial, market, judicial/quasi-judicial review, constituency relations and professional accountabilities including sophisticated networks of independent regulators and Ombudsmen. Thus, accountability has many relevant dimensions, and a noticeable casualty in the international privatisation movement may unfortunately have been public accountability. Ministerial responsibility has clearly reduced - hardly surprising when one of the key objectives of privatisation in the first place was to 'free up SOEs' from political influence and control. But the legal process of privatisation itself can risk stripping away many of the broader accountability mechanisms that operated in the public sector - Ombudsman review, Freedom of Information and scrutiny by the Auditor General (Taggart 1992) in the absence of explicit government accountability initiatives to combat this. The accusation here is that privatisation hollows out the state (Rhodes 1994, 1998).

Overall then, managerial accountability may increase, but at the cost of a decrease in

the broader public accountability mechanisms, with questionable accountability impacts on customers. There has also been a sense in which the accountability guardians have changed with divestitures. The traditional assumption of Ministerial accountability has been replaced by a strengthened role for an independent network of regulators for privatised activities as well as more attention to specifications through enforceable contracts for services and infrastructure. As Herb Simon argued, a strong democratic society needs a dispersal of power, not one dominated by private business interests (to run government), or powerful governments (to corrupt democratic processes) (Simon 1997). What is certain is that we are now much more focussed on questions of accountability than we have ever been in the past. This in itself may well promote better performance. With PPPs, highly complex contracts also provide only limited opportunity for meaningful levels of transparency or public participation. As well, complex adjustment formulae and contracts lasting up to several decades can result in a lack of clarity as to agreed arrangements as well as reducing the capacity and flexibility of the crown to make future decisions in the public interest. There has been little discussion about how the various current roles of Treasuries can be best balanced - policy advocate, project promoter, financial steward, regulator and trusted parliamentary adviser.

A further central issue in privatised activities is openness and the extent to which disclosure of information is affected. Worldwide, transparency of the privatisation process or transaction has been an ongoing concern, and plenty of examples provide case studies of failure, here (Kikeri et al 1992, World Bank 1995, Wiltshire 1990). Just as important as the privatisation process, though, is the question of the extent to which the



openness of ongoing operations is affected. On this score, UK research (Thompson 1993, Heald 1989) concluded that the disclosure of information declined following privatisation of the electricity supply industry whilst Australian research on electricity privatisation concluded that accountability had improved (Hodge 2004). In many jurisdictions the over-use of commercial-in-confidence in private contracts has been an ongoing concern. A common risk with all privatisation programs through history has also been the allegation of corruption. And whether such allegations are proven, doubts over corruption and cronyism are likely to linger when reformist governments create an atmosphere of less openness in the availability of information.

## Conclusion

Privatisation is a family of techniques with a long pedigree, and has become a central policy solution for governments over the past three decades. Paradoxically, the long history of government-business relationships has not been well acknowledged in the rush to apply private sector techniques and practices within government. This article has looked at four major components of the privatisation family; enterprise sales, the contracting-out of government services; public-private partnerships; and the philosophy of private sector development strategy (PSDS) in developing countries. With each of these four components, a mix of evidence as to effectiveness in meeting privatisation objectives has been found. Divestitures have worked best where markets for services have been created as well as changing ownership, and where strong competition and regulatory frameworks have ensured benefits for citizens. Likewise, contracting-out public sector services has resulted in some benefits on average, but has also not worked for all services. Public-private partnerships, the latest chapter in the privatisation story, have been

more controversial in their application to public infrastructure and services, and like their privatisation family cousins, have also witnessed mixed empirical evidence as to effectiveness thus far. Private sector development strategy was seen as the broadest of these components, and covered a wide range of development goals and aspirations. One central and recurring theme in all areas of the privatisation family of meanings has revolved around issues of accountability in governing today's privatised state. In particular, there continues to be a real challenge in ensuring that the expectations of citizens for continued public accountability are properly met as states progressively privatise.

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## Privatisation and Governance

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### **Introduction**

“The word “privatisation”... is used in two senses. In the narrower sense, it means the transfer of assets hitherto owned by the state into private hands. The broader interpretation covers the property relations in the economy as a whole, so that privatisation of the economy means that the share of the private sector grows until it ultimately becomes the dominant economic sector” (Kornai 1995:32). An extension of the broad definition provides us with more insight. Besides the selling or leasing of public property, the term further implies the abandonment of any government control over all units of the economy, as well as the abandonment of the state monopoly in certain sectors. It also includes the return of property that had been illegally confiscated to its rightful owners, the promotion of private enterprises, and the effort to attract foreign investors.

The broad definition may also be called “the restructuring of the independent and private sectors.” (Hare 1994:34-35). The creation of small private firms may, eventually, achieve the revival of the private sector, even without the help of the privatization of state firms, (Koves 1992:40) or in other words, privatisation represents the transfer of state-owned assets to private ownership, alongside the creation and fostering of de novo private businesses (Hare and Canning 1994). Privatisation is an alternative way of distributing and choosing means of generating wealth. Consequently, it may also be considered as a distribution of political and economic power in the long run.

Especially in the context of former communist countries, Estrin (1996) views privatisation as a “*reversal of communism*”, considering the restoration of the private

property rights which are essential to a free market economy. In the same sense “the emergence of a de novo private sector using the fixed assets of former state owned firms purchased after bankruptcy or liquidation, can lead to industry-level supply responses to demand changes even in the absence of supply responses from current and state owned firms” (Estrin 1996:2).

The broader meaning of privatization incorporates the restructuring of the economy as a whole, including the mentality of entrepreneurship, and the profit seeking under private ownership. Besides the privatization of municipal and state firms that were small or medium-sized and facilitated in a way the tangible privatization observed in the everyday life of the citizens in the Central and East European Region, the creation of new firms is also essential for the total development and expansion of the private sector.

### **Reasons and Cost-Benefits**

A justified question is why privatization is necessary for advanced western countries and why it is so vital for countries that are transformed into market economies. The answer lies in the social, economic and political aspects of the country. An examination of all the reasons for privatization is essential for the understanding of the concept, for the identification of the goals of privatization, and for the choice of the appropriate method(s) for each country.

Privatization assists the creation and promotion of a competitive environment through the termination of monopolies, the creation of new small private firms and the passing of state companies into private hands. The individual/private owner is a better producer than the state, because the individual’s goal is profit maximization. As a result, the privately owned firm will try to

satisfy a larger percentage of the market, adapting to the consumer tastes and needs.

“The government is not a good manager of economic resources or a good monitor for the assets it entrusts to others, and does not provide motivation for managers and employees in order to increase production” (UN 1992:213). For example, in a centrally planned economy neither the central authorities have the incentive for a good governance of the state-companies, nor do the managers aim to maximize profits, manage effectively, or encourage innovations, etc. It is difficult for the state to monitor and control the managers, as managers may pursue their own interests rather than those of the state’s. Estrin (1994:15) pointed out that “even if they had the appropriate skills and experience, such managers rarely have the incentive to restructure their organizations for competition in world markets”.

The socialist economy has no rational criteria for the effective allocation of capital, something that can be efficiently achieved by privatization. Private ownership will impose stricter control on the management, and hard budget constraints for the creation of extra revenues. Private owners recognize the necessity to upgrade and update the technological and management capacities and lifestyle of the companies, and introduce new corporate governance “incorporating” in the new range of products the increased needs and demands of the citizens.

The state will be relieved by the burden of financing the deficits of loss making state owned enterprises (SOEs). The development of the private sector will assist the development of financial markets, which in turn, will assist with the financing of new investments, through the creation of a stock exchange market. This way, companies may find cheap capital, formerly provided, in many cases, by the state.

The effect of privatization, for example, in transition economies is crucial for employees’ motivation, since their abilities are judged according to their work and not according to their connections with the government. Under these circumstances, entrepreneurship and innovation are encouraged, and productivity is increased (Aslund 1991:19).

The creation of a healthy market will provide solid ground for further advancement of trade that will create a substantial market and may even attract foreign investment. The revenues from the sale of state assets and the saving of financial capital formerly given as aid to loss-making state companies may be used to cover the budget deficits or other governmental priorities such as social policy. Another source of revenue that will assist the state financially is the taxation from the new or transformed private firms’ revenues (Estrin 1994:17).

As privatization means more and different owners, and an increased number of producers, we have increased competition, more options, and more choices, and large number of products with wider varieties for the consumers. Consequently, better quality and most probably better and lower prices.

Privatisation along with the clearance of property rights, the liberalisation of the market, the elimination of monopolies, and the increase of competition is a necessary step for planned economies to grow into successful market economies. There are imposed taxes on profits for privatized SOEs, so we have increased state revenues.

Civil servants are not entrepreneurs. Public sector organisations are bureaucratic and not run in a way that will give profits needed to run and expand a business. Private firms and private owners become accountable to their shareholders and their desire for profit. Private enterprises are run on commercial rather than political grounds.

Losses incurred by the enterprises will accrue to the company and not the taxpayer.

Privatization breaks down monopolies into more competitive industries and thus competition is introduced into the markets. Private properties guarantee the efficient use of resources and eliminate shortages (Marangos 2004).

On the other hand, privatisation simply creates private sector monopolies with many barriers for new firms entering the industry. Privatised firms make decisions based on commercial profit maximising grounds. Nationalised firms make decisions in the interests of the public. The state runs companies for the benefit of consumers; private companies will run their companies for a profit. Privatising strategic and profitable industries means that government revenues will be diminished, as profits are directed to the shareholders, as in the case of multinationals abroad. Lower government revenues may mean lower government spending on education and health.

Privatisation can be seen as selling off the nation's assets which the public, through taxation or work have "bought" and developed over the years. The production and distribution of certain goods and services like medical care, education, water, and electricity, especially for poor people, should remain in the hands of the state. The state should also intervene in the market in terms of offering social security and welfare benefits. People have a basic right to enjoy basic goods or services without the state considering the cost it will have to pay.

Privatised enterprises are sold at very low prices. Privatised companies take less heed of social costs. Prices (after privatization) may be raised, whereas in SOEs the government has full control over prices. In the short term and during the restructuring process, it is possible to have an increased unemployment rate.

### ***Methods of Privatization***

Generally speaking, there are two distinct ways of privatization. The first is *commercialization*, which refers to the transformation of state companies to joint stock companies that in due time offer their stocks for privatization through the various methods described below. When commercialization involves changes in management structure and working rules, it is also called *Corporatization*. This conversion is an intermediate stage before the enterprise ownership and control can be transferred into private hands.

The other way to privatize a state company is *liquidation*, a method involving the sale of separate assets of a company to different investors, and one preferred for the privatization of small-scale enterprises.

A discussion of various means of privatising government functions follows. Eleven methods stand out.

#### ***(a) Sale through Auctioning.***

The transformation of state property into private property can take place by auctioning state enterprises and selling them to the highest bidder. In this way, all individuals have the opportunity to become owners at real market prices. Foreigners can also participate as long as some guidelines are imposed to protect the country's interests. This protection policy, however, should not be based on isolationism or xenophobia. An obstacle to be overcome is that the financial assets of the local people in developing or transition countries are not adequate to purchase state enterprises. This problem could be solved by the state providing loans to finance the purchase of state enterprises (Marangos 2004:587).

#### ***(b) Sale through Financial Intermediaries.*** This involves the transfer of ownership of



enterprises to financial intermediaries whose ownership structure may consist of pension funds, worker and/or management funds, citizen funds, or private financial institutions such as banks and government agencies. The advantage of this method is that it is quick and can be viewed as equitable. However, a loss of government revenue is involved. On the other hand, in the transition countries there is a shortage of experienced financial managers operating in a market environment who can administer these financial intermediaries efficiently (Marangos 2004:587).

*(c) Sale through Vouchers.*

This is actually the distribution of some amount of capital to private hands, enough to purchase state assets. This capital is distributed in non-transferable equity such as vouchers that are only valid for purchasing state owned assets. In most countries that this method took place, the distribution was equal among all the population, but in some countries nationalistic matters against ethnic minorities have interfered in the fair allocation of vouchers. Another determinant of this method is the 'rules' for the use of the vouchers. Some tactics observed in different countries are: (a) the direct trading of vouchers for company stocks (Czechoslovakia), (b) the trading of shares in government funds for the joint ownership of the formerly state owned assets (Poland), (c) the option of exchanging the vouchers for housing and assets other than firms (Latvia, and Slovenia). The mechanism of the exchange should be determined as well in terms of timing, or rights to assets (manager-employee buyouts, free to everyone, etc.) [Estrin, 1995, pp8-10].

The mass privatisation method is used more and more after its success in several countries. The **advantages** of such a method are the speed of privatisation and the equity in

the distribution, avoiding the accumulation of wealth and thus power to the nomenklatura, honouring, in this way, all citizens. As Estrin (1994:23) says: *"In this way, voucher schemes can give a popular legitimacy to privatisation itself, for example by returning assets to people from whom they had originally been confiscated or by giving the general population a stake in the assets accumulated through forced saving in the communist era."*

Other advantages are the elimination of the need to find local buyers and the creation of instant 'players' for the stock market. Furthermore, it is a very low cost method for the state to administer. Mass privatisation is also contingent with the common public dislike of foreigners since much of the privatised companies remain under local control. It is a fact that mass privatisation accelerates privatisation, correcting in a way the potential delay in market privatisation. It also accelerates the establishment of social securities funds, and meets with the desire of the state for broader participation of the population.

One of the main objections to mass privatisation is that it requires the existence or creation of financial infrastructure, including financial intermediaries, pension funds, mutual investment funds, investment banks, a stock exchange market and a securities commission, prior to the implementation of the plan. Other drawbacks are that it generates minimum income for the government and that the wide range of parties involved foster fraud and financial speculation. Moreover, it creates problems in the governance of the firm, and does not provide any aid to the state since it lacks compensation for the government and fails to generate money-capital for restructuring. Although many argue that mass privatisation does not require the evaluation of assets, it is essential that each citizen receives vouchers

not only of equal number, but also of approximately equal value. The effort to fairly evaluate the companies and other operational problems may cause delays or postponement in the process (still, it is much quicker than other methods). The wide distribution of the shares may prevent the establishment of a firm ownership, thus maintaining the company's problems in terms of effectiveness and managerial monitoring. In a mass privatisation model, citizens "acquire" the vouchers free or for a trivial price. Thus, they are likely to view the vouchers as "free lottery tickets", believing that they actually have nothing to lose if the company they acquire faces failure. This notion makes most citizens behave rather indifferently towards their investment. The mass privatisation method is sometimes perceived as a way for the government to indirectly admit the failure, or insufficient success of the market privatisation.

*(d) Management and Employee Buyouts (MEBO).*

A company can be acquired by the existing management of the company (MBO) or by the combined forces of the employees of a company (EBO) who can have the control in the respective company when acting as a group of individuals. Usually EBO and MBO are supported by some financial institutions. MEBO is a method combining the employee buyout (EBO) method and the management buyout (MBO) method. MEBO was established mainly in the Central and Eastern European countries (CEECs), either as the only means of privatisation of a company or combined with other privatisation methods. MEBO is facilitated with preferential policies for employees and management such as the lower purchasing price of the shares or the payment of the shares in instalments, the higher dividends or preferential credits specifically for them, etc. MEBO is not only

favoured by the employees and managers, but by the governments as well because it is simpler and faster than the standard privatisation methods and it assists to hinder the resistance often posed to the privatisation process by managers and workers against privatisation that might threaten their job security. This method creates the less valuation problem since the interest in the price of the privatised company that is 'sold' is minimal and the objective is not the creation of the maximum possible privatisation revenue.

MEBO, though, has some negative effects, specifically on a company's efficiency. Initially, MEBO privatisation rarely eliminates the lack of funds of the companies due to the favourable payment agreements (sale price) mentioned above, which are provided by most of the Eastern European countries' legislation. Moreover, if the price of the company is trivial, then the workers or the managers risk very little. Consequently, the danger arises that not much effort will be put in the efficient operation of the company, returning this way to a loss-making company. The state, however, can minimize the effect of loss making companies by imposing hard budget constraints and clear bankruptcy laws.

Another danger of the MEBO method is that employees and managers will support the undervaluation of the company in order to purchase it at a cost significantly lower than its real value. If this happens, the method turns into "wild privatisation". Still, another drawback is that, under the employees' ownership, the process of reducing the number of human resources of the company either as a form of cutting expenses or restructuring, is a matter not easily decided. Lastly, reinvestment of earnings is supposed to suffer, since a common policy is to allocate the revenues to the labour compensation.

*(e) Leasing.*

For some state assets, where privatization is not desirable or possible due to the high risks involved, privatization can take the form of leasing state property to individuals. As long as the lease or rent is market-determined, this will result in the productive exploitation of resources, as well as the creation of the preconditions for transforming these assets into private property (Marangos 2004, p588).

*(f) Liquidation.*

For unsuccessful enterprises that can not be restructured and for shares of companies that can not be sold, the government can initiate liquidation proceedings and sell the physical assets owned by the state enterprise. This process would facilitate the reallocation of resources to the most productive activities (Marangos 2004:588).

*(g) Initial Public Offering (IPO).*

An IPO is the process of offering for the first time shares of a company, private or state owned, for sale to the public. The potential investors are invited through advertisements in the national press to subscribe to the company's shares. This method is used either when one or more shareholders wishes to sell their stake(s) in the company or when the company wants to raise capital by issuing equity or debt. In this privatisation process, the major shareholder (the state) desires to sell its holdings in a particular company.

Under the IPO-PLUS scheme, private interests are allowed to establish special investment funds called Privatisation Investment Funds (PIFs) in order to buy the shares of enterprises being privatised. The PIFs issue their own Public Participation Shares (PPS's) to the public. These participation shares are issued at a uniform low price to ensure broad public participation. To initiate the program, private interests form management companies.

*(h) Return to 'Real Owners' (Restitution)*

The concept of this privatisation method is to return the assets to the parties that used to own them before communism. This may sound legitimate, but it needs much consideration. First, there is the procedural matter, who owns what. This is a decisive problem that took place in the CEE countries. At least a generation passed under communist regime, and the initial ownership may have been divided, or the property may have been enriched by value added by the state. Moreover, there might not be real evidence of the former ownership status.

This method is very slow and complicated. Since during the period of communism, all citizens contributed equally to the state assets, then how can one claim to be the sole owner of an asset on which value was added during communism? Another issue that arises is that since the distribution of wealth was unequal before communism, the restitution may also be unequal today, leading the majority of the population to poverty in times that are difficult. A better way of returning wealth to the real owners is to offer the approximate value of the formerly owned assets in the form of government funds, as was the case in Hungary. In countries where there was actual return of assets, including Bulgaria, the process was very slow and provided little help to the economy (Estrin 1995). The success of the restitution process depends on the existence of the past owners, of the appropriate documentation and political judgement.

*(i) Spontaneous Privatization.*

This is where the managers or the state are authorized to issue stocks, transform a SOE into joint-stock company/ies, and sell them to anyone interested. By allowing managers in place or self-management councils, enterprise or workers councils to turn existing firms into corporations, these autonomous firms were to

become fully responsible for their own financial health (UN 1992:231). Usually the state requires the auditing of the firms' assets, and at least one major investor, holding at least 20% of the shares. At the end, the company and the state share the profits. This method of privatization is the one that will bring the fastest results, but it will also leave many 'doors' open for suspicious or even illegal exploitation, such as biased deals and under-evaluation of assets. The "insiders" are likely to have a far better idea of the true value of the firm than the authorities, and are therefore likely to be able to obtain a very good price. Problems of this sort led to a public outcry against so-called spontaneous privatization, even in highly pragmatic Hungary which therefore introduced fairly strict state supervision of the privatization process" (Estrin 1994:25).

*(j) 'Wild Privatisation'.*

Quiet, underground, illegal, mafiasation, hidden, nomenklatura or wild privatisation is a model rather than a method of privatisation. It is the informal mobility of information that favours the people who have inside connections in agencies and firms, and allows them to obtain assets in informal and illegal ways, usually assisted by external capital. The favoured parties are state bureaucrats, managers, rulers of the former regime and very rarely, workers. In this way, the nomenklatura exchanges the political power they had during the regime with financial power at the expense of both the state and the citizens, and continues the uneven distribution of wealth and the delay of social efficiency.

One should make the distinction between the 'insiders', who are the people inside each firm, like managers and workers, and the 'outsiders', who are every other citizen local or foreign. Another element with which we can distinguish the privatization methods is

the control mechanism of the procedure; whether it is centrally controlled by the government, or de-centrally by an independent agency supervised by impartial experts such as well-known consultant companies who evaluate assets and set the rules. If the procedure is centrally controlled by central courts, then the procedure is very slow and requires a long period to bear results. Still, there is more clarity in any transaction and avoidance of 'wild privatization'. The decentralized control is a quicker, more efficient way, but more vulnerable to personal interests and corruption. The control mechanism may adopt features from both ways in order to assure better results. An example is the model that transfers the ownership to institutional investors, like privatization funds or banks and insurance companies, who, in turn, start trading shares. This third way necessitates the existence of a stock market [Meyer 2000, pp268-269].

*(k) A creation of small, privately owned firms.* Privatisation from below is also a 'method' of privatisation in the broader sense. In many countries this practice helped the recreation of the private sector, especially sectors like construction, local retailing, trade, and services, preferring trade rather than production. These firms are created from scratch or through reinstitution and other privatisation methods. The emergence of small firms shows a development in entrepreneurship. Most of them have been relatively successful despite their vulnerability to heavy taxation, corruption and crime, and to the lack of infrastructure (Brada 1996:75-76).

As a conclusion, the choice of privatisation method depends upon the specific characteristics of the country and usually countries use combinations of

different methods in order to achieve efficiency in the privatisation procedure.

Kornai (1995:34) commenting on the return of property, compensations, solution of the restitution problem, selection of the mass or voucher privatisation method, and the manager's or employee's buyout, argued that all the above may be used for political reasons (to collect votes for the coming election by creating a favourable image for the party in power).

### **Speed in the Privatisation Process**

The speed of introduction and completion of a privatisation plan is very crucial in the privatisation process. The concepts of gradualism and gradual speed in the privatisation programme and the restructuring process, as well as the concept of shock-therapy or big-bang and the rapid speed in the privatisation, are the two main approaches that can be used, either separately, or combined in different stages of the privatisation process.

An alternative speed of privatisation is the stop and go or trial and error speed of privatisation process. Accordingly, the government proceeds in the announcement of a concrete plan of privatisation process. However, during the achievement of this plan and the successful closure of a few privatisation deals, endogenous and exogenous factors prevent its completion or a provisional freeze, befalls or even yet provisional postponement of the remaining deals occur due to the political cost of the proposed privatisation deals (e.g. various reactions of citizens, increased unemployment rates, a delay in the appearance of the positive factors that results from the finalised deals, or government inability to succeed in privatisation deals, etc.). Furthermore, divergence in the privatisation program, or a small delay in the achievement of the deals (either through

gradual or shock therapy) does not alter the speed of the process, changing it into the alternative of "stop and go". Sometimes and on purpose, the ultimate goal of the privatisation plan is not announced.

Rapid privatisation is favoured by some countries, but it has sometimes been criticized by theorists. Fischer Stanley (1992:227) has concluded that "small firms should be privatised by sale almost immediately... larger industrial firms should be corporatized as soon as possible...plans envisage the corporatization phase being completed within a year or two... the key to the long-run transformation of the formerly socialist economies may lie less in the privatisation of the very large industrial firms ... than in the development of new firms and the growth of existing smaller firms... for that reason, rapid progress in other areas, such as the creation of a suitable legal environment, price decontrol ... is as important to the development of a vibrant private sector as privatisation of large firms".

The characteristics of 'big bang' favour fast privatisation techniques including mass privatisation plans, leaving the task of restructuring to the owners of the privatised firms. On the other hand, others object, especially in the case of privatisation of state owned firms, that the rushed moves have often led to the disorganization of valuable operational enterprises, a fact assisting the drop of the output level (Fischer 1992).

Dornbusch (1991) argued that radical change is the only realistic option, and gradualism opens the door to an unstructured free-for-all market: consumers will go to the black market and firms will produce for the black market. A temporary collapse may be inevitable, one way or the other, but in the context of radical reform it may at least be the seed for reconstruction. Transition needs to be accomplished extremely fast because the distance to go is far and the task is

overwhelming. The illusion that transition could be accomplished over many years is just that, an illusion. A gradualist solution is appropriate when a market economy is in place, and the issue is how to improve the use of resources at the margin. Dornbusch for example concluded that this is not the case of Central and Eastern European economies. Therefore, a radical and rapid reform is the right remedy.

Fischer Stanley et al. (2000:1) mentioned that *“the faster is the speed of reforms, the quicker is the recovery and the higher is growth”*. Lipton and Sachs (1990:77) argued that a rapid transition to a market economy with a heavy emphasis on economic integration with Western Europe is needed.

Lipton et al. (1991:231) argued that “In Eastern Europe, privatisation is a very difficult task, involving nothing less than the complete redefinition of property rights for literally thousands of enterprises ...Advocates of rapid privatisation are typically confident that even if quick privatisation initially leads to an inappropriate distribution of ownership with, for example, too diffuse ownership, or firms in the wrong hands, then the capital markets will encourage a reshuffling of ownership through takeovers, mergers and buy-outs so that there is a proper matching of owners and firms...”

The shock therapists are in favour of the immediate privatization of state owned enterprises through restitution, liquidation, auctions and free distribution of vouchers. Conversely, neoclassical gradualists are in favour of a slower pace of privatization through liquidation and auctions (Marangos 2004, p589).

Regarding the speed of the privatization from an empirical point of view, we can safely infer that after the first decade of a transition process, privatization should be accomplished in a more gradual manner, and it should be preceded by enterprise

restructuring along with the creation of an adequate institutional framework (World Economic Outlook 2000). On the same line, Laban and Wolf (1993) argue that a more gradual strategy is beneficial, because a “big-bang” approach involves significant financial risks for a government. The limit of social acceptance as regards to the level of transformation costs that should not exceed a certain threshold level (indicated by huge output decline and a high rate of unemployment) should be considered as well. Spicer et al (2000) argue that rapid mass privatization destroys the old system of central planning, but does not build the institutional settings that facilitate the restructuring in the postprivatization environment. They advocate that by implementing a gradual reform process, new institutions will evolve gradually from the economic and social relations intrinsic to the initial post-communist economic environment. Furthermore, Rosser and Rosser (2001) maintain that gradual privatization is more appropriate, as they believe an increase in the speed of privatization leads to a rise in the level of corruption and underground economy, resulting in negative outcomes such as insider takeovers and corrupt asset stripping.

Castanheira and Roland (2000) researched the optimal speed of transition from a state-owned to a private market economy, in respect to the closure or restructuring of state-owned enterprises (SOEs). By applying a benchmark general equilibrium model, the authors infer that if the closure of the SOEs is too slow relative to the optimal path, the resources left to new enterprises will be limited and the speed of transition will be reduced because of the fewer investments made and only if, SOEs are subject to hard budget constraints, the optimal speed of transition will be achieved. On the other hand, if there is an excessive rate of closure

of inefficient SOEs (a case that happens early in the transition process), the speed of transition will be reduced. This means that policies aiming at accelerating the speed of sectoral reallocation might have negative outcomes. A more gradual approach is also upheld by Rider (1994), who asserts that a speeded-up process will favor established interest groups (with their associated political links) and will encourage the establishment of monopolies.

### **Sequence of Privatisation: Dilemma of Restructuring Before or After Privatisation**

Regarding the sequence in the restructuring and privatisation process, first of all, property rights should be clear, and the governments should overcome the restitution problem. Furthermore, very clear laws and market-friendly laws that clearly define individual rights and responsibilities and embody market friendly economic policies should be introduced and enforced without discrimination. On the other hand, constant changes in the legal framework should be avoided. Moreover, sound institutions should be introduced and monopolistic markets should be abolished. Formal institutions that include judges, arbitrators, prosecutors and court functionaries should be established, so that laws become effective. Political commitment to transparent privatization outcomes ought to exist, combined with the elimination of bureaucratic systems and more incentives should be given for new companies to be established in the country with no governmental interference. Finally, changes in the financial sector, such as the introduction of a stock exchange market, and investment and pension funds, along with the introduction of bankruptcy rules and hard budget constraints are also necessary.

In the consideration of sequence, a decisive question that arises is whether a

country should *privatise before or after restructuring* or should both proceed simultaneously. Another question yet is whether there is a need for sequencing in privatisation or not and if so what principles should underline it.

Since the question of whether privatization ought to preside or follow restructuring emerges, the definition of restructuring is needed. Restructuring "...is a multidimensional, encompassing: "reactive" policies brought about by the hardening of firms' budget constraints (e.g. labour-shedding, wage reductions, plant closures); strategic aspects, including export reorientation, changes in the mix of products and changes in management structures; and "deeper restructuring", generally involving substantial new investment, that can deliver large improvements in enterprise performance and growth over the long run" (EBRD Transition Report 1995:128).

Restructuring may also be viewed from a macroeconomic perspective. As companies restructure by adopting policies and strategies that increase their efficiency, governments restructure by adopting laws, regulations and policies in the same direction, in hopes of increasing the efficiency of the state economy. In the macro economic sense, the adaptation of companies to new market standards is also restructuring (Hunya 1997:275).

There are three kinds of restructuring: physical, organizational and financial that may be used separately or in combination, depending on the needs of each company. Physical restructuring involves the updating of the physical elements of a company, like the introduction of new equipment of higher technology and generally changes in the production facilities, like shifts to another production site. Organizational restructuring involves the improvement of the management in all aspects of the company, like marketing,

human resources, etc., but also improvement in strategic decisions concerning the operation of the company, such as potential joint ventures or other forms of co-operations. Financial restructuring refers to the rearrangement of sources of capital in a way that best suits the needs of the firm. This kind of restructuring includes, in the case of state owned-firms in countries in transition, the termination of state subsidies, the restructuring of the internal and external debt, exploration of other sources of capital, and generally the establishment of financial autonomy.

If the state decides to undertake restructuring prior to privatizing the firm, it needs to spend additional capital time and effort on the company, in return for a more successful presentation of the privatization deal as well as higher revenue from the sale. On the other hand, if it avoids restructuring, the state achieves quick privatization and is relieved of the burden of financing the loss-making company. Restructuring before privatization holds another, hidden, drawback. The managers and employees of the company under restructuring procedures will probably be ill-motivated to participate in the restructuring given that, in the long run, they risk the possibility of losing their position in the company. What governments may fail to consider is that the restructuring they intent to apply on a company may be far from what the potential investors expect. A close inspection of the company should determine the way that is more profitable for the state. Sometimes the government uses restructuring as an excuse to delay privatization in order to avoid the political burden of mass dismissals of employees and generally to stall hard restructuring methods by the new owners. A long restructuring period allows room for corruption and increases the possibilities that the

nomenklatura will profit by wild privatization.

All methods of privatisation need different implementation periods and may be applied before or after the restructuring of a firm.

*Slow privatisation* is where most of the state companies will be restructured and sold, only after the domestic savings are adequate enough for purchasing the larger percentage of the state owned assets, or when the offers from foreigners are large and lucrative enough. Usually there is a delay for the sake of increased revenues from the sale or from the search for a strong enough strategic investor, who will transfer know-how and other positive spillovers into the host economy.

*Rapid privatisation:* the country aims to privatise all companies either through inviting foreign direct investments (FDIs), or through vouchers, before they are restructured. This requires at least 2-4 years.

*Mixed privatisation:* selected privatisation methods for selected state assets that aim to quickly privatise 25-40% of the total state assets in three years and 90% of the total state assets in seven to ten years.

## Conclusion

Private property is the foundation of market economies. Without private ownership the market cannot exist and vice versa. The privatization of state property has a lot of objectives, such as: to guarantee the efficient use of resources and eliminate shortages, to provide revenues to the government, to stimulate the restructuring process, and to entice foreign investors to become active participants. At the same time, privatization has its drawbacks - the creation of private sector monopolies, the increased unemployment, the fact that it takes less heed of social costs, and many others.

The *speed and sequence* of the introduction and completion of a privatisation



plan are very crucial in the privatisation process. A decisive question that arises is whether a country should privatise before or after restructuring or should both proceed simultaneously. To this dilemma there is no clear answer. The choice of privatisation method and privatisation procedure depends upon the specific characteristics of the country. Countries usually use combinations of different methods in order to achieve efficiency in the privatisation process.

The Central and Eastern European countries have used several methods in order to resolve the above problems in the optimum way for both state and citizens (Bitzenis, 2003). Needless to say, most of the methods did not bring about the expected results, and the privatization process has proven to be an extremely complicated and difficult task for the transition countries (Estrin, 1995, p8). Thus, the dominant method of privatization should depend on specific characteristics of the country in question, and on value judgments with regard to equity, sequence, and speed of privatization.

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### **Introduction**

Public Administration is not a novel societal institution, but it was modern society that pointed out the importance of having a properly organised and regulated civil service, capable of enforcing the law in an unbiased way and supporting economic and industrial development. The term “bureaucracy” has usually attracted negative sentiments, being perceived as the rules of professional bureaucrats, alienated from the remainder of society. The term “bureaucracy” stems from the Greek word ‘*kratos*’, meaning the “rule” and the French term “*bureau*” meaning the “office”. Initially, the term was used to describe the rules of the office and the people who made them. However, besides this fairly pejorative meaning, the term has also been interchangeably used to refer to public administration, civil service or a country’s public services apparatus. As with many other words, the meaning will be determined by the context in which they are used. Comparative public administration consequently means the study of bureaucracy, or civil service system, as they exist in different countries. Traditionally, bureaucracy has been linked with the existence of the state and the civil service (public administration) serving as an administrative apparatus of the executive, but with the emergence of numerous international organisations, especially in recent years with the “redefinition” of national sovereignty and prevalence of the international order. The emergence of supranational organisations with an extensive administrative apparatus that is becoming omni-potent, with ever increasing jurisdiction over the national member states, the overall picture is becoming even more complicated.

However, even the term “public administration” is not exclusive. In British terminology “civil service” is used to describe the government’s administrative apparatus. The Civil Service is a political term which has different meanings in different countries. Historically, the term emerged in the late 18th century in order to make the distinction between civilian and military personnel of the East India Company (Drewry and Butcher, 1988). Over time, this meaning evolved towards the contemporary concept which states that the civil service, at least in the British *domain*, means “the remunerated personnel, other than those serving in the armed forces, whose functions are to administer policies formulated by or approved by national governments” (*Blackwell Encyclopedia of Political Institutions*, 1987:104).

This term is different (at least in the British and US concepts) from “public service”. Public service includes civilian personnel employed by defence forces, army officers seconded to “civilian posts” out of the armed forces, the judiciary (public prosecutors, judges, magistrates, etc.), local government employees and other people employed by governments at all levels of power (e.g. educators in some countries, traffic wardens, firemen, etc.). Usually, there is a problem of how to classify police officers and (regular) employees of civilian intelligence agencies. Formally, they should be civil servants, but since their activities are regulated in a rather specific manner, they are usually exempt from the civil service category and belong to the larger group—“public service”.

The public sector has grown constantly since World War Two and this trend remained more or less unquestioned until the 1980s, when the developed countries asked the question of whether one can get more out of the traditional public sector and what ‘value for money’ really is referring to

services received. The leaders of the reform were primarily Anglo-American countries and the movement was labelled “New Public Management” (NPM). This move, that was strong in Australia, New Zealand and the UK, aimed at downsizing the public sector and ensuring that citizens were put in the centre of the changes. As the movement was widely endorsed around the world, it was a primary force behind the convergence of public administration systems and “globalisation in public administration” if such a thing can exist. NPM reforms have again been nationally coloured and embraced the different interpretations of the major characteristics of reform.

This paper will present the major developments in comparative public administration research and then we will focus on developing a broader theoretical framework for the comparative research. We will then compare the main civil service systems and classify them into recognisable groups. We will look at value systems in public administrations and then look at different issues that have attracted and may still attract public administration comparative research in the future, questioning to what extent globalisation trends may have influenced the convergence of various public administration systems.

### **A Historical Sketch of Developments**

The study of comparative public administration has traditionally been based primarily in Europe, as in the US, the study of “comparative government” meant comparing the US model with other countries and putting the American government in a comparative perspective through anecdotal reference to foreign (‘alien’) experience and practices (Chase et al 1980). Within the European context, comparative public administration generally meant comparing national bureaucracies and looking for

determinants that may be the same or similar in a number of countries. American attempts in the 1960s, however, tried to make a “grand theory” of public administration, but primarily focused on developing countries (see Riggs 1964; Heady 1966). In the 1960s, the study of public administration was primarily dominated by the functionalist theoretical approach (see: Mills, 1959). The theoretical models developed may have survived the test of academic coherence and consistency, but they have failed to influence the practice and assist in empirical research. Consequently, in the 1970s, the comparative study of (national) bureaucracies was strongly criticised, and fell out of fashion (see: Ilchman 1971).

However, the 1970s had a fashion of their own, looking for other innovative models of public administration, attempting to create a model of New Public Administration (Cahoon 1972, Frederickson 1976, 1980), which only administrative historians and some public administration students remember. In fact, as in many other academic disciplines, every decade had a particular theoretical bias and attempted to develop a break-through model that would explain a particular social phenomenon. As we can see, the public administration theory had not fallen short on this either. In the 1980s, the behaviourist approach dominated. A noticeable number of comparative national studies were conducted, with the extensive use of quantitative methods. The most notable work in this phase was written by Aberbach, Putman and Rockman (1981), based on research conducted in the late 1970s. While the 1960s were focused on producing an omni-potent and omni-applicable theory, the early 1980s were marked by research that was based on producing cumbersome, detailed and data-bursting case studies of national democracies, preferably based on a research protocol developed to allow cross-cultural

comparisons. As these studies were predominantly focused on data and had bias towards detail, it was difficult if not impossible, to produce studies that would engulf all the issues in national public bureaucracies. Rather, the studies focused on particular issues (politico-administrative relationship, bureaucratic elite(s), financial position of civil/public servants, etc.) facing national public administrations. The studies produced offered vast amounts of information but did not lead to theory building.

The studies produced in the late 1980s offered rapprochement between theory and practice depicted in heavily data-biased empirical research. The most notable contribution was made by B. Guy Peters (1988). Other contributions include Rowat (1988), Dwivedi and Henderson (1990) and Farazmand (1991), although the legacies of the 1960s development public administration and functionalism could still be seen (Heady 1984; Caiden and Caiden, 1990). There were also attempts to address the position of top political appointees (ministers) in comparative perspective (see Blondel, 1985). Another noticeable attempt to study comparative bureaucracy was made by the University of Indiana which organised, in 1997, a conference on “*Civil Service Systems in Comparative Perspective*” where a number of case studies were produced on national civil service systems from around the world. The theoretical framework embracing a number of issues was presented in a volume edited by Bekke et al (1996) Important case studies have been prepared by Verheijen (1999), Bekke and van der Meer (2000), Burns and Bowornwathana (2001) and Halligan (2004).

Besides these multi-country projects, there was a number of projects that compared civil service systems/public administration in two countries (Muramatsu & Naschold 1997, Christensen & Peters 1999). Also, the focus

of comparative bureaucracy research in the first years of the 21<sup>st</sup> century has been placed on the issues of the increased politicisation of the civil service (Verheijen 2001; Peters and Pierre 2004). It certainly seems that the 21<sup>st</sup> century will be marked with similar trends to the 1980s and early 1990s, when the focus was on studying various aspects of public bureaucracy in a comparative perspective. However, the question remains open as to what the variables that have to be considered in comparative research are. Literature does not fall short in offering a number of variables to be considered. Heady’s (1966) seminal work emphasised the relationship between political appointees and professional civil servants and the role of public administration in (economic) development, as important variables. In the 1980s, Peters (1988) was of the opinion that public employees, organisational structure and bureaucratic behaviour are the most important conceivable dependent variables in comparative public administration research. Pierre (1994) put forward the following three variables: politico-administrative relationship, intra-organisational dynamics and the nature of the relationship between the public administration and the wider civil society. Identifying different variables is important in defining and developing a theoretical framework for further research.

### **Developing a Theoretical Framework: Setting the Stage**

Developing a sustainable theoretical framework is not the only problem facing comparative public administrations. Public administration (public bureaucracies) are heavily embedded in national cultures, regulated (until now predominantly) by national laws and regulations, with internal organisational cultures which are, to a large extent, nationally defined and all these characteristics make the comparative research

more complicated than was expected. However, two-country comparative studies (Muramatsu & Naschold 1997; Christensen & Peters 1999) have proven that there is often enough common ground to conduct good comparative studies. The first step would be to define all the institutions that are to be studied in a comparative perspective. It is necessary to clarify what we mean by “public”, what an “organisation” is and what is regarded as the public sector, public bureaucracy etc. (Peters 1992).

Civil service systems are predominantly influenced by the national legal system and the characteristics stem from, to a large extent, the tradition to which a legal system belongs. There are, of course, more similarities than differences between the countries and national legal systems that belong to the same legal family (Anglo-Saxon vs. Continental European legal tradition). Larger, more inclusive classifications, however, address only some of the problems. There are outstanding problems with measurement and theory testing. If one has a problem defining what the public sector is, then it is impossible to measure efficiency and effectiveness of those institutions. Comparative research requires minimum common ground on all the institutions that will be addressed in the comparative research. The results reported in evaluation and implementation research can be of great help in defining the methodological agenda in comparative public administration research.

When one develops a research agenda for research on comparative bureaucracy, the main problem is to define a number of aspects that depict the relative civil service systems and ensure that there is a common denominator which will allow successful comparison. For (public) bureaucracy to exist, the state must be in place. Bureaucracy is often perceived as a synonym for the state, especially in Continental Europe, where the

public administration is to secure the continuity of the state, whilst the politicians are “deciduous” (Šević & Rabrenović 1999). Bureaucrats are somewhat ‘evergreen’ in contrast to the politicians who have a limited life span, dictated by political cycles. Nevertheless, defining the bureaucratic apparatus does not resolve the problem of the very notion of the state. Socialist thinkers will claim that the very essence of the state is to exercise (physical) power and keep the social order intact (protecting the ruling class or classes); others may see the state as a social contract (Rousseau), or simply a network of institutions performing necessary social functions; linking the state and the law in one monolithic body (Kelsen). The state is to promote certain interests (Jessop 1990, Nordlinger 1981), either domestically or at an international level (Krasner 1978).

Public administrations have traditionally been very national. They differ greatly by the nuances of the legal system (despite the fact that they may belong to the same legal culture, as we will see later), their recruitment policies and practices (elitist or socially inclusive), group values, organisational culture and informal networks for resolving intra-conflicts, etc. All these variables must be treated fairly seriously when the national legal system is described and analysed. National settings differ in how comprehensive public administration is. The terms “civil service”, “public service” and “public administration” may be used interchangeably, but the content of each term may differ. Usually, public administration includes core government services, whilst the public service may refer only to non-core services offered to the government, or be used as a generic term for all the services rendered by the government (the state in the Continental European legal context). In Japan, the “public sector” refers to the core government services and will not include the services offered by

government-owned enterprises. This is the reason why any comparative research usually has to start with a proper definition of the terms and what each of them entails, regardless of the fact that it may be self-explanatory in itself.

Comparative public administration research has to focus on both similarities and differences between different national administrations. It is necessary to develop an awareness of the endemic differences between public administrations across the world. Second, it is necessary to see that comparative research is focused on a group of countries and not only focusing on developed countries, whose experience has been traditionally used in the design of the public administration systems in developing and transition countries. However, in practice, the vast majority of civil service systems belong either to the European or Anglo-American group. Nevertheless, these two groups are not as monolithic as they may seem at first sight. There are significant differences between the British and American public administration, although one has to admit that globalisation has brought about more convergences, not only between the groups, but also amongst the groups. The British Civil Service remained less traditionally politicised than the American and the relationship between the public administration and the legislature in the US and the UK is fairly different. Certainly, confronting the two groupings of public administration systems is very useful in furthering the framework for comparative research.

### **Public Administration: European vs. Anglo-American Concept**

The very concept of state in Europe and Anglo-Saxon (Anglo-American) countries is different. Whilst the public administration in European countries is created to serve the state, the civil service in Anglo-Saxon

countries serves the government of the day. In Continental Europe, a civil servant should remain loyal to the State, while in Britain civil service is “On Her Majesty’s Service” and a civil servant is seen as a servant of the Crown. There were long debates in British history over what this really means. It seems that the words of Sir Robert Armstrong, at the time the Head of the Home Civil Service, depicted the situation very aptly:

“Civil Servants are servants of the Crown. For all practical purposes the Crown in this context means and is represented by the Government of the day. There are special cases in which certain functions are conferred by law upon particular members or groups of members of the public services; but in general the executive powers of the Crown are exercised by and on the advice of Her Majesty’s Ministers, who are in turn answerable to Parliament. The Civil Service as such has no constitutional personality or responsibility separate from the duly elected Government of the day. It is there to provide the Government of the day with advice on the formulation of the policies of the Government, to assist in carrying out the decisions of the Government, and to manage and deliver the services for which the Government is responsible. Some civil servants are also involved, as a proper part of their duties, in the processes of presentation of Government policies and decisions.” (House of Commons 1985-86:II:7)

In the presidential system, the national bureaucracy must keep fairly good relations with the legislative body, besides following the orders of Presidential political associates, who formally head different governmental departments. But, it should be also noted that the US Congress has its own administrative staff, which is different from those employed by the executive branch. In a parliamentary system, the civil service is not as segmented. Civil servants can be deployed within any



government department, as well as holding posts in Parliament. And, the main employer is the same - the Crown or the State. This is the reason why, in a way the government and parliament are, for civil servants, politically appointed superiors. Therefore, there is an argument that the nature of a parliamentary government is more about seizing control of the entire *apparatus* of government, and then using the apparatus to implement a party programme (Rose 1987; Katz 1986). It is believed that due to such “a strategy” the administrators have to be more loyal and the responsibility for policy is much clearer in a parliamentary regime, compared to a presidential one (Pasquino 1986). Namely, the government must ensure that there will not be any failure in policy implementation, due to sabotage or to a lack of commitment amongst civil servants. In some parliamentary systems, civil servants can choose to support a notoriously partisan project, but this will clearly disclose their political bias and they would be required to quit when a new government comes into power. In the German system, the institution of “early retirement” supports this claim. Also, in the parliamentary system, accountability is employed through ministerial responsibility. The minister is solely responsible for all the successes and failures of his/her employees, even for the mistakes made by the regular, permanent staff.

Theory singles out the British system as the best representative of this model of responsibility (Marshall 1989), although some adjustments have been made, especially in the 1990s making the British model no longer quite so “pure”. Scholars would point out that both ministers and Parliament have contributed to this change. Ministers achieved this by disclosing those civil servants whose performance was subject to certain irregularities (Woodhouse 1994), while Parliament established a number of committees to oversee departments (Drewry

1985). In a number of parliamentary regimes, the institution of the *ombudsman* has helped to establish a practice of civil servants’ individual responsibility. But, in cases in which *mala fidae* cannot be proved, ministerial responsibility remains the main way of handling a problem.

In contrast, in a presidential system, the accountability of the Public Administration is twofold. The administrators are responsible to their superiors in the department, as well as to the committees and sub-committees of the legislative body (the Congress, in the US case). Political responsibility remains in the hands of a minister (a Secretary in the US), but his/her civil servants can be summoned to give evidence before a committee or sub-committee of Congress at an open hearing. Civil servants can be asked a question related to the current management, or whether he/she noticed any mismanagement in the Department. However, they should not be asked questions on current government policy. From the European perspective, this kind of enquiry can be seen to be a close supervision of Public Administration by a legislative body, which can seriously affect the overall performance of the Civil Service. Civil servants can become less effective, being concerned that mistakes can be severely penalised by outside bodies (Legislature). Usually this close supervision brings a risk-averse structure and behaviour associated with it into day-to-day reactive responses, and in a fast changing environment the Civil service can be very slow to respond, thereby increasing social costs.

However, on the other hand, this kind of close link with Congress in the US helped to develop national bureaucratic apparatus in which its members are much less likely to follow orders or instructions, which they believe to be immoral, illegal or threatening to the interests of national security etc. In the presidential system, an individual civil servant can be legally pursued for his actions. But,



there is the question as to what extent the rules are respected and implemented. In continental European countries, theory makes a distinction between the *legal system* as a logical harmonic set of (legal) norms and *legal order*, which entails social behaviour under the legal norms imposed. In Anglo-Saxon legal theory this distinction is not so clear and legal order has more generic notion. Public administration is clearly an important element of the state (Rockman 1992), but each public bureaucracy has its own legal rules, recruitment patterns, intra-organisational dynamics, group spirit, organisational cultures and different patterns of interaction with outside stakeholders (clients). It should not be forgotten that the public administration apparatus is the main instrument of interaction between the elected politicians (seen here as rule-makers) and the wider civil society. Public bureaucracies have different kinds of relationships with politicians; different immediate values that they have to endorse in different national political systems; and different perceptions of their social functions. In Anglo-Saxon countries, the public administration serves the government of the day, while in Continental Europe, the loyalty is towards the fairly ephemeric concept of state (Hall & Ikenberry 1989, Jessop 1990, Kranser 1984, Lane 1993, Skocpol 1985, Rockman 1992).

### **Comparative Public Administration: Considering the Values**

Public administrations (bureaucracies) are driven by various principles. In Continental Europe, the public administration framework is dominated by the concept of the *Rechtsstaat*, Weberian model, based on public law; whilst the American model is a model of “public interest”. It seems that the majority of other models are in fact modifications of these two models, with some departures that are often attributed to the national culture, characteristics and collective social

experience, etc. The model initially introduced, proved to be very strong and difficult to de-root even in extreme social circumstances. For instance, the Japanese bureaucracy has been modelled after the German Imperial civil service, with full mimicking of German public law. When Japan was occupied by the Allies, but *de facto* American forces after the 1945 defeat, the victors wanted to introduce a more American-like model of society. In many domains their aims were achieved, but not in the domain of public bureaucracy. Even today the Japanese bureaucracy is similar to the German one (Muramatsu and Naschold 1997), although there are many very Japanese national characteristics embedded within (Miyamoto 1994). The focus on the *Rechtsstaat* guarantees that the bureaucracy will ensure the existence of the state where the rule of law will be observed. However, the problem is that in German history there were times when the concept of *Rechtsstaat* was applied, but with ‘modifications’. In Nazi Germany, everything was subsumed to the Leader (*Führer*) and all societal institutions were to follow the Leader unquestionably (Schmitt 1932). This was still formally done within the concept of *Rechtsstaat*. This brings us to the next point of focus. One ultimate task is to assess to what extent the written law is applied in the country. Developed countries with a long history of democracy have strong cultures and traditions of obeying the law, whilst developing countries usually have a very poor record in law enforcement. This is why there is a world-wide trend to introduce performance indicators which should demonstrate the efficiency and effectiveness of the public administration, especially in relation to the public (general public). Another variable that is increasingly important in studying the national public administrations is corruption. Corruption increases the total social cost and imposes additional transaction costs on citizens and

other interested parties (Šević 2002). This also increases the feeling of social insecurity and finally leads to serious (or systemic) institutional failure. It is almost impossible to consider the operation and the state of the national civil service without considering the systemic shortcomings in operations and the level of corruption experienced.

The possibilities for comparative research rest with the focus on personnel practices, as they are usually strongly supported by national values and perceptions. Some public administrations are elite in their very essence, recruiting the vast majority of new staff from top national universities, or where a degree from the top national university is required for the promotion to the top echelon of the national civil service. For instance, in Japan the vast majority of top civil servants come from the University of Tokyo (*Tōdai*, or *Tōkyō Daigaku*, in full), and in the UK the majority of British senior civil servants traditionally came from the University of Oxford. The situation has significantly changed in both countries where the civil service is encouraged to expand its recruitment base. However, this is not typical for Japan and the UK only, as in many countries the national university or universities are usually perceived as the major proliferators of future bureaucrats, with regional and local universities playing either a secondary or having no role at all. Nevertheless, the broadening of the recruitment base is perceived in many countries as an important element of public sector reform and it is expected that the trend will continue. It will be necessary to ensure that some of the informal prohibitive practices are also removed and not only formal avenues opened to aspiring future civil servants.

The national public administration system is a sub-system of the national political and social system. As such, it is exposed to the main elements of the national culture. Social preferences will be reflected upon and

imported into the values developed by the civil service. Hofstede's work on world cultures is an interesting point of departure in that kind of research (Hofstede 1980). Whether certain values are upheld by society or not, may be reflected on the public administration. For instance, if society observes the law, it will be difficult to picture widely spread corruption in the national public administration. Despite the overall trends of globalisation that tend to spur convergence of the public administration systems, one may expect that "national specifics" will still play an important role in shaping the national public administration systems.

### **Politico-administrative Interface and Organisational Dynamics**

The relationship between politicians (political appointees) and career civil (public) servants has traditionally been the focus of research (Aberbach et al 1981). The nature of the relationship between the public bureaucracy and elected (or politically appointed) officials effectively determines the discretion that the public administration has in the process of policy implementation. The politicisation trends in the public administration have attracted attention in Western European political science/public policy theory since World War Two. The perception of the executive power as politico-executive and administrative-executive branches, strengthens the importance of administrative policy making for the elected (and election driven) politicians (Rockman 1992), who are, by definition, seeking re-election.

Theory has delineated a number of models to describe the nature of interface between career civil servants and elected political appointees. Aberbach, Putman and Rockman (1981) suggest that there are four principal models of the said relationship, within the range, from an ideal model of highly distinctive political and bureaucratic roles to

the model where the roles more or less converge. Peters (1987) classified this relationship into five possible models covering the same range as Aberbach, Putman and Rockman (1981), but using more memorable language (for instance one of the models was named '*functional village life*'). The nature of the relationship between politicians and civil servants is not only defined by law (or other formal rules), but also depends on the practice, social expectations and overall political context in which the political system operates. The increase in relative importance of delegation for policy decision making and policy implementation (Thatcher & Stone Sweet 2003), may have a profound influence on future developments in the relationship models. However, future developments will be manifold and might well encompass the redefinition of the general public's views of public administration. Administrators may, in the future, be given the power, not only to implement, but also to define policy, within the *a priori* agreed limits.

The focus on the organisational structure and inner organisational dynamics will also be important in any comparative research of public administration. Organisational structure can be seen as a key for the explanation of bureaucratic behaviour, intra-organisational power scheme, administrative efficiency and/or the communication flows within the administrative organisations (see: Pfeffer 1978). The organisational structure (organisational setting) can be perceived either as an independent variable or a dependent variable to be explained for instance, by extra organisational power relations, such as the one existing between the legislative and executive powers, or various stakeholders in the public policy process (see Moe 1989). The organisational setting provides the stage on (or within) which different political and administrative factors

realise their roles. The organisational design enables the administrative organisation to relate to its environment and to model effectively intra-organisational distribution of powers. The traditional national public bureaucracies are perceived to be fairly rigid structures, with little, if any, room for innovative behaviour. However, with the introduction of recent public sector reforms that promote the introduction of business-like practices, the situation has been changing significantly. Modern national public administrations, especially in developed countries, are more prone to support innovative behaviour, stress the importance of organisational learning and knowledge management capacity for the increase of their overall capacity to deal with current social issues. NPM driven changes have certainly contributed, not only to more flexible civil service systems, but also to their convergence and the increase in the similarities between the systems that, for a long time, have been regarded as diverging.

Still, one may make a clear difference between the *Rechtsstaat* and "public interest" underlined public administration system, or between the French and German sub-model, but the application of NPM will eventually lead to the convergence of the model where cross-fertilisation will bring one or more hybrid models of public administrations. Hopefully, these hybrid models will be more effective and efficient, with a citizen as the main focus; not affecting adversely the level of democratic development recorded by the countries in question. On the other hand, this also raises the question of the end of comparative public administration research. This question, however, will be answered in the future by positive practices.

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## Public Administration Theory and Perspectives

*Jack W. Meek*

### **Introduction**

Should public administration be concerned with theories of management? Theories of politics? Theories of institutions? Theories of groups? Theories of individuals? Theories of administrative context, global and local? It is the position of this essay that the answer to these questions is “Yes”. Public Administration is an eclectic field and theories that influence the curriculum, the study and management of public affairs are derived from various established and evolving fields in the academic disciplines.

Today, Public Administration is informed by an even wider set of valuable inquiries that seek to make the field relevant. Chaos theory, as an example, which was born out of mathematics but is finding relevant application and attention in a wide variety of areas including public administration (Kiel 1993, Overman 1996, Newell & Meek 2000). As a result, it is difficult to set universal boundaries clearly identifying the field, especially that of public administration. Void of any singular theory or for that matter any set of theories that uniquely characterize the field, Public Administration remains a professional field of practice with a diverse academic background and diverse interests directing its future.

The purpose of this essay is to suggest that the field of public administration has an extremely broad contributing base. The leading scholars of public administration have found various ways to organize the field, including categorical frameworks presented in an edited summary of the classics in the field by Jay M. Shafritz, Albert C. Hyde and Sandra J. Parkes (2004), and by outstanding interpretations of the field, as found in the

works by H. George Frederickson and Kevin Smith (2003), Robert Denhardt (1993), and Michael Harmon and Richard Mayer (1986). This essay simplifies the voluminous contributions to the field into three areas or “domains” in order to provide a fundamental typology of public administration scholarship along with some selected contributions and references. The idea behind constructing a simple typology is to offer an orientation to the field. But there are various problems with such simplification and the reader is asked to review other approaches to understanding the field of public administration through the references cited in this essay.

As a preliminary step, we examine the role and function of theory. What do we mean by “theory” when we refer to the study of public administration? What is the role of theory in the study of public administration? What are the theories of public administration? It is no easy task to address these questions, as answers to them tend to be dependent upon the individual providing the responses. As it goes, different individuals, given different perspectives, will have different responses.

### **Theory and Evolution of Public Administration Theory**

Given the different nuances of the domains of public administration, you may not be surprised to find that there are many definitions and types of theory. For some, the functions of theory are to describe, explain and predict phenomena (and thus prescribe solutions). For others, there will various designations of theory that are related to the varied purposes of research, including Normative (what ought to be), Empirical (observable and measurable), Grand (overall guiding perspective), Mid-Range (narrowed focus or perspective of patterns), Descriptive (characteristics of a subject), Prescriptive (what actions should take place), Instrumental (functional or utilitarian operations), Formal

(mathematical), and Applied (useful knowledge in practice). The role, contribution and advantages of theory are also related to the purposes of research. Overall, the scholar and practitioner benefit from theory, as theory aids in selection, collection, ordering and storing of data; enhances conceptual and methodological clarity; specifies and builds relationships; attempts to transcend time and space; represents a form of explanation; represents a form of prediction; and provides provocative force (Frederickson & Smith 2003).

As to the role of theory for professional studies, the pressing need is for practicality and to assist policy-making. The words of Laurence Lynn illustrates the demand for theory in the practice of management, as follows:

“The role of theory in the professional field of public management is to assist managers and their advisors in bringing critical, analytical intelligence to bear on the design and choice of institutional arrangements for achieving the goals of public policy. Theories enable managers to say (or hypothesize) why observed actions, behaviors, and results occur (or may occur) and to prescribe arrangements that may lead to intentionally better governmental performance. Theory in public management ... will draw upon academic disciplines concerned with explaining behavior and choice.” (Lynn 1993:13)

Critical issues within public administration that center on the continuing debate over the role of the state complicate the role of theory. One's position on this political and philosophical issue will also determine one's interest in the role of theory. The point is that one's position on theory and practice in the

study of public administration rests on an a priori assumption about the role of the state: is the state to be limited or all encompassing. The best deliberation over this issue can be found in the work of Richard Stillman, II (1991), in his work, *Preface to Public Administration: A Search for Themes and Direction*.

As to the definition of theory, there is continuous debate. For some, *theory is a proposition or set of propositions that seeks to explain or predict something* (Frederickson & Smith 2003, Lynn 1993, Bill & Hardgrave 1973). Drawing from this definition, knowledge development in public administration is based on testing theories. A different definition of theory is based on pragmatic consideration with regard to relationships and contextual situations: the best theory is one that allows for one to develop and enhance the situation of oneself and others. Here the work on action theory by Mike Harmon (1981) is illustrative. In this perspective, theories are viewed as part of action-orientation and knowledge development takes the form of actions that have received deliberative attention. This is a very different perspective that the theory testing perspective and we will return to these points at the end of the paper.

Prior to addressing the areas or domains that have affected the development of Public Administration, an interpretation as to how the field has emerged is in order. According to Donald F. Kettl (1993), the field has undergone four stages.

The first stage was *Centrality of Administration* (1887-1915), where administration was established as playing a central role in the political process of government; writers such as Woodrow Wilson and Frank Goodnow were explicit in their discussion with regard to a professional administration especially an administration



separate from the political spoils and corruption.

The second was *Scientific Management* (1915-1940), the era of the establishment of scientific management and administrative principles and “one best way” to perform administrative work and where the leaders of public administration sought to carry out their administrative work separate from the politics associated with the nationally elected leadership. The aim was to create a science of administration that would improve government and would not be subjected to the changing tide of electoral whims.

The third stage, *Critical Self-Examination* (1940-1969), emerged after the war where behavioralism, the study of individuals and not institutions, took root. Behavioralism initiated a separation between those interested in knowing how to improve the structure and practice of administration and those interested in the process leading to the separation between political science and public administration. The emphasis on seeking a unique understanding of the theory and practice of public administration with a focused emphasis on the intersection of administration and democracy lead to the creation of a new professional association of public administration—The American Association of Public Administration (ASPA)—and to a new professional journal, the *Public Administration Review* (PAR)

And the last stage is *Centrifugal Forces* (1969-Present), a period characterized as a generation of centrifugal forces based upon new approaches including implementation, public management, and the use of economic theories. These centrifugal forces exacerbate the politics-administrative dichotomy by emphasizing one over the other and often masking their interconnection. There is little compatibility with these decentralizing trends.

These stages reveal the long-lived politics-administration tension that seems part of the nature of the field: administrative systems are central to a professionally managed state; but political systems can distort the efficient management of state practices. The significance and study of this phenomenon have developed into various perspectives or schools of thought about the central questions to explore. It is these perspectives that we can explore later, as perhaps they best suggest priorities for theory expansion. It should be understood, however, that public administration is a complicated subject matter, and what has been termed an “intellectual crisis” or “identity crisis” (Ostrom 1974, Sillman 1991) is reflected in the dual nature of public administration: theory AND practice. Focusing on one will limit the advancement of the other and vice versa. Yet this tension should be a celebrated point as it provides a constant source for inspiration and exploration and makes way for a larger appetite in the search for meaningful practice and theory. The central theme of this essay is that *what* the researcher in public administration focuses upon (managerial and organizational processes or administrative and policy influences) and *how* they approach their subject (testing or developing theories) defines their goal of research and the relationship that research has with theoretical concerns. And there is plenty of excellent research to draw upon that reflects these practices in public administration research.

### **Domains Informing Public Administration**

This paper offer three simplified areas or domains of study in public administration: (1) Organizational and Management Theory; (2) Policy and Administrative Theory; and (3) theories contributed from the various disciplines of the Social Sciences. The first domain emphasizes subjects related to the

study and management of organizations and the understanding of behavior within organizations. The second domain emphasizes subjects that are related to policy interests (however derived) and the role of public institutions in achieving those interests. It is Dwight Waldo, probably Public Administration's most renowned theorist, who placed the critical feature of public administration as, "Administration may be thought of as the major invention and device by which civilized [people] in complex societies try to control their culture, by which they seek simultaneously to achieve—within the limitations of their wit and knowledge—the goals of stability and the goals of change." (Shafritz & Hyde 1987). The third domain, emphasizes findings or insights that are derived from other fields that inform either organizational or policy understanding. Within each domain various sub-fields (sometimes disciplines themselves) are identified as contributing areas of inquiry to these domains. The reader should interpret no particular ranking of importance to the order in which these domains are listed.

As mentioned earlier, it should be emphasized that the logic to classify the fields that affect the study of public administration is an endeavor that carries many problems. What to emphasize or to organize around says much about the writer and the goals a researcher may have with regard to the role of the state, the role of professional administration as well as their personal experience and background, which influence their thoughts. Previous books on theory have all used different typologies in order to stress different frames of reference to serve analytic purposes (Frederickson & Smith 2003, Denhardt 199; Harmon & Mayer 1986).

### **Organization and Management Theory**

One domain of inquiry that has influenced the study of public administration is the field of

organizational theory. This is an enormously broad field characterized by a very wide selection of subject matter. Simply classifying the field of organizational theory is a task that finds many alternatives. Jay M. Shafritz and J. Steven Ott (1992) in their edited work, *Classics of Organizational Theory*, list eight different authors in how each have organized the field, then offer one of their own. In addition, the authors point out that organizational theory, "draws significantly from such diverse disciplines as sociology, psychology, social psychology, cultural anthropology, political science, economics, business administration and public administration (Shafritz and Ott 1992, p. 3)." The same is true for public administration as it draws from organizational theory as well as the other disciplines. No one argues that organizational theory is a discipline, but it is a domain to which various disciplines contribute and from which various areas of study can draw upon, such as public administration. For example, there are public administration scholars who write about organizational theory, such as Robert B. Denhardt (1993) Mike Harmon and Richard Mayer (1986) and Harold Gortner (1987) and David Carnevale (2003). There are also those from other fields who write about organizational theory that is used in the study of public administration, such as Amitai Etzioni's, *A Comparative Analysis of Complex Organizations* (Etzioni 1975). Often in this field, the nature of public bureaucracies is not the central focus of attention, but rather the focus is on organizational behavior in general terms. Organizational and administrative theories typically represent prescriptive efforts to improve organizational functioning in both "private" management theory and public management theory (Marrow 1980).

The field of management, like organizational theory, has a long history and

is characterized by a similar set of various schools of thought. Management theory is characterized by its more prescriptive nature but it is still influenced by organizational theory. Often the contributors of management theory are the same as organizational theory, such as Henri Fayol (1940), Chester Barnard (1938), Henry Mintzberg (1979) and Jay Lorsch (1969) among so many others. The schools of thought associated with management theory, according to Harold Koontz, in his work, "The Management Theory Jungle,"(1980) are as follows: (a) The Management Process School; (b) The Empirical School; (c) The Human Behavior School; (d) The Social System School; (e) The Decision Theory School; and (f) The Mathematical School.

#### *Public Management.*

Public management is a major segment of the broader field of public administration and is concerned with the functions and processes of management in agencies at all levels of government as well as the nonprofit sector. Public management focuses on public administration as a profession and on the public manager as a practitioner of that profession. It is concerned more with the internal operations of a government agency or nonprofit organization than with its relationships and interactions with other departments of government, a legislature and its committees, the courts, or organizations in another economic sector. Public administration is a broader term than public management, "because it does not limit itself to management but incorporates all of the political, social, cultural and legal environments that affect the managing of public institutions." More specifically, public management addresses the organizational "how to's" of implementing public policy. "Planning, organizing, and controlling are the major means by which a public manager

shapes governmental services. Thus, public management focuses on the managerial tools, techniques, knowledge, and skills that can be used to turn ideas and policy into programs of action (Ott, Hyde and Shafritz 1991:1-2)

Laurence E. Lynn (1993) outlined five critical "concepts" as the theoretical foundations for the study and practice of public management: (a) Principle-Agency Theory, (b) Market Mechanisms, Hierarchies, and Cans, (c) Bounded Rationality and Cognitive Style, (d) Executive Discretion and Bureaucratic Supply, and (e) Logic of Collective Action and Game Theory. Each of these theories is to be used in designing strategies and formulating policies for public organizations. He continues with five additional concepts that can improve the critical analysis of public managers: Reframing, Networks, Psychological Type, Garbage Cans, and Tools Assessment. Combined, the concepts, according to Lynn, provide a powerful set of theories to improve public management. In his words:

"Theory-based or analytical practice of public management will not always be superior to instinctive practice, value-driven practice, or "rules and checklists" practice, but it offers the best hope for systematically transcending the often stifling effects of ego, ideology, inertia, ignorance, and the unexpected on governmental performance." (Lynn 1993:15).

What is referred to as "new public management" embraces the use of market strategies, economic incentives and public choice logic as a way to improve efficiency and effectiveness of public institutions in the delivery of public services. In this area of thinking, the central idea is to link the organizational priorities in public administration decision-making with the

evident self-interests of both those who implement and receive public services (Kettle 2000, Osborne and Gaebler 1992).

### **“Practice” of Management.**

There are those authors who are concerned with a more “how to” approach to the study and practice of public administration. Perhaps represented best in the mission of the American Society of Public Administration (ASPA), these authors are concerned with the rather many diverse challenges that face public administrators and their need to cope with those challenges in practical ways. The accumulation of knowledge is based upon practice and is codified in periodic publications. Accumulations of this scholarship appear in James L. Perry (ed.), *Handbook of Public Administration* (1990) Jack Rabin, Bartley Hildreth and Gerald J. Miller’s *Handbook of Public Administration* (1989) and Barry Boseman’s *Public Management: State of the Art* (1993).

Related to the practice of management, there is a substantial body of work that is concerned with the role of the public administrator as a central feature in the seeking of administrative thinking that includes ethics and justice in addition to efficiency and rationalization that is informed by the science of decision-making. It is the role of public administrators to be self-reflective (Harmon 1995, Schon 1983, McSwite 1997) and enhance social construction that would legitimize our public institutions (Terry 2003) that have lost connection to citizens because of an over-reliance on modernist logics and strategies (Fischer 2000, Yankelovich 1991, Argyris 1993). The argument here is that technical rationality and professional expertise that characterizes the behavior modern administrative state, overpowers and ignores the realities of citizens who not only have meaningful ideas to offer, but, if included,

could provide valuable insight into improving public service. This insight is not honored by the modern administrative state.

### **Policy and Administrative Theory**

Another domain of public administration theory is the area of public policy that has as a tradition a focus on bureaucracy blended with a study of the political policy process. Theories that have evolved from this field of study focus primarily on the policy process: problem identification and agenda formulation, policy adoption, policy implementation and policy evaluation. Much of the work includes analysis of actors involved in the policy process, such as legislatures, executive branch, administrative agencies, the courts, interest groups, political parties, research organizations, media, citizens, etc. There are six areas of theory development that characterize theories of public policy, listed below:

#### *Theories of the Policy Process*

Noted authors in this field include: James E. Anderson (1990), Charles E. Lindbloom (1993), Thomas Dye (1992). Much reliance on theories refined or developed in political science are discussed in this literature, such as systems theory, group theory, elite theory, institutionalism, and rational-choice theory. An interesting contribution in this field is the blending of political science and public policy theory with management techniques and theory. This was done in the work of Grover Starling, *Strategies for Policy Making* (1988). His work represented a unique blend of various disciplinary techniques so improve the field of policy making for the practitioner.

#### *Implementation*

Implementation study, according to Donald Kettl (1993), began as a field exploring government failure, something quite contrary to the approach of traditional public

administrationists. The field has developed to look to comparative processes and variations of outcomes. Examples of scholarship that represent some of the most known theories include: Pressman and Wildavsky, *Implementation* (1973), Mazmanian and Sabatier, *Implementation and Public Policy* (1983) and O'Toole, "Policy Implications for Multi-Actor Implementation"(1986).

### *Public Budgeting*

It is difficult to place the field of public budgeting within the context of public policy alone and it easily bridges to public management as well. It is listed here because of the influence of Aaron Wildavsky's, *The Politics of the Budgetary Process* (1964) and the enormous impact that work had on the study of the budgetary process, namely that budgets are the by-products of political interactions and need to be analyzed as such. Current work in the field emphasizes PERFORMANCE BUDGETING stressing explicit and measurable links between policy objectives, budgetary outlays and program performance (Kelly and Rivenbark 2003).

### *Program Evaluation*

Another area of study that has taken on disciplinary-like dimensions is the area of program evaluation. Evaluation studies as a field goes well beyond public systems and includes all areas of human and organizational activity. According to Rossi and Freeman, *Evaluation: A Systematic Approach* (1993), there are three major classes of evaluation research: program design, program monitoring (and accountability) and program utility (impact and efficiency). There are a wide variety of qualitative and quantitative methodologies that can be designed to address evaluation. The most noted work in the field of public administration in Eleanor Chelimsky's, *Program Evaluation: Patterns and Directions*

(1989). This latter study discusses six different types of evaluation approaches routinely conducted for program evaluation. An excellent source for fundamental approaches to evaluation can be found in the edited work of Joseph Wholey, Harry Hatry and Kathryn Newcomer (1994) and in Barry White and Kathryn Newcomer (2005).

### *Policy Evaluation*

Policy evaluation is separated from program evaluation in that the intent is to explore policy alternatives and to go beyond mere program evaluation. To understand and embrace intended and unintended policy consequences calls upon a broader framework of analysis to be considered. The most significant in the area of policy evaluation is that of Frank Fischer who developed a multiple-layer accountability framework to understand policy evaluation (Fischer 1995). Other contributors to this area of analysis include classics like Ann Majchrazak, *Methods for Policy Research* (1984), William N. Dunn, *Public Policy Analysis: An Introduction* (1981), Stuart Nagel, *Public Policy: Goals, Means, and Methods* (1984). The most recent work that brings a post-positivist perspective to policy analysis is that of Goktug Morcol (2002) and Peter Bogason (2000). It is these contributions that stress the limits of positivist approaches to policy analysis and the need to respect not only the limits of policy analysis that is based on positivism, but to incorporate those limits into policy deliberation.

### **Governance**

Making a rather dramatic emergence in the field of public administration is the recognition of new forms of collectives and organized participation in public administration (Goldsmith and Eggars 2004). So dramatic is the explosion of participation in various forms of networks, public-private

partnerships, quasi-autonomous organizations that the field is offering the use of the term, “governance,” to improve the description of patterns of interaction that is emerging in the various arenas of public administration (Lynn 2000). B. Guy Peters (1996) has assisted the field with articulating four variations of governance possibilities: (1) market government characterizes centralized governments are in need of seeking market based reforms and efficiencies in service provision; (2) the participatory state is one that focuses on the need to break down hierarchical top-down structures by emphasizing participatory management and the inclusion of citizens in governance; (3) flexible government where the capacity of governmental agencies ability to respond to environmental challenges is enhanced beyond traditional patterns or habits; and (4) deregulated government where governments are allowed to find creative, effective and efficient solutions that are not found in the traditional bureaucratic top-down models constrained by restrictive rules. While the term governance has several meanings, the essence of the term means that government can be conceptualized in various ways and that government is no longer the central player in public administration even though it remains a critical player (Frederickson 1997).

### **Disciplinary Fields Informing Public Administration**

Political Science is the academic home and chief parent of public administration. The sub-fields that contribute to public administration are many, including political theory, comparative politics, and international relations. An elaboration of the theories which affect the study of political philosophy are beyond the scope of this essay, but are critical in discussing the foundations of the role of the state. The more contemporary theories, and the authors which represent

them, which have dominated the field of political science include: Systems Theory, Group Theory, Game Theory, Pluralism, Elite Theory, Incrementalism, Theories of the Policy Process, Rational Choice Theory, Institutionalism. Political philosophy is also an enormously potent area of contribution related to the purpose, design and functions of public administration (Rohr 1986; Harmon 1995; Fox and Miller 1995).

Economic theories have had an enormous impact on the study of administration. There are three various types of economic theory that have influenced public administration interests: Economics for Policy Analysis, Political Economy, and Public Choice Theory. Chief among the contributors to economics as policy analysis are Edith Stokey and Richard Zeckhauser's *A Primer for Policy Analysis* (1978) where they examine various economic tools (queuing theory, simulation, markov models, benefit-cost analysis, valuation of futures, discounting, linear programming) in application of policy choices. The political economy approaches are characterized by the use of economics in addressing how well services are to be created and by what institutions. Similar to policy analysis, these approaches raise questions about the role of the state and provide theory in addressing the role of the state. An example of this work is David L. Weimer and Aidan R. Vining's, *Policy Analysis: Concepts and Practice* (1992).

Another dimension of this field would be the various contributors to the study of how the American economy is managed and a more philosophical discussion on the consequences of economic systems (Okun 1975; Dahl and Lindbloom 1963; Galbraith 1973; Heilbroner 1967) As to public choice theory, according to Kettl (1993), the works of Buchanan and Tullock, Tullock, Downs provide a cogent set of predictions from a limited set of assumptions (rationality) of

participants in a political processes seeking to maximize their utility. Kettl (1993) outlines four branches of theory that have emerged with regard to models of bureaucracy: Principle-Agent Theory, Bureaucratic Outcomes Theory, Institutional Choice Theory and Transaction Cost Theory each of which has contributed greatly to the understanding of public bureaucracy relationships, how choices are made, and what determines choices.

From sociology, Public Administration owes much to the classic works of Talcott Parsons and Edward Shils (eds.) *Toward a General Theory of Action* (1962) and Max Weber's, *The Theory of Social and Economic Organization*. (1947) Psychology and social psychology have also long held a central position in the study of management. Industrial psychology contributed greatly to earlier management thought and continues to play a major role today. Modern leadership theories are often based on psychological foundations, and much research on upon learning and conflict styles developed in psychology. Other theoretical contributions include the following works: Irving Janis (1972), Morton Deutsch (1973), and David Kolb (1984).

### **Public Administration Perspectives**

There are two dominant perspectives on Public Administration theory. Each has a different view as to the role of social science epistemology, research methods and knowledge expansion. Each perspective has a different view on the role of the three domains of public administration theory. In one perspective, the *positivist perspective*, "the" scientific method has played an enormous role in the development of the social sciences, including the study of public administration. The basis of social science comes from traditional scientific methodologies adapted to the study of social

phenomenon. The theories that play large in forming the basis of scientific inquiry included logical positivism and rationality. The logic behind the acceptance of such approaches rests in the fields of mathematics. There is a valuable base of literature that represents the fields of modern methodology relevant to the study of public administration and management (Kaplan 1964; Kerlinger 1973; Nachmias and Nachmias 1992; Kuhn 1970).

Indeed, the idea of a science for public administration was the initial proclamation of Woodrow Wilson (1887). An understanding of the role of rationality plays a critical role in the analysis of decision-making where many authors have found other patterns that describe outcomes that are not predicated on rationality (Simon 1997; Allison 1971; Janis 1971; Zey 1998). In this perspective, public management theory offers the scientific method as a critical tool of inquiry; policy and administrative theory can be viewed as testable propositions from which we can deduce meaning, and interdisciplinary theories provide transferable logics from which we can enhance our interpretation and prediction of public administration behavior and action.

From another view, *the action perspective*, there is an important role of theory that is pragmatic in meaning and application. The work of Charles Fox and Hugh Miller, *Postmodern Public Administration: Toward Discourse* (1995) finds significance for students and scholars of public administration in the creation and maintenance of discourse. The Fox and Miller version of discourse seeks to identify public administration not as a uniform framework of public implementation that seeks efficiency as its noblest cause. The version they seek is the understanding of public administration as a deeply contextual adventure. Their work certainly connects with the public

administration tradition of Follett (1924) Dewey (1927) and its insights rest in ideas that were fostered as a result of its contextualizing focus: that citizens count, that discourse matters, that relationship matters.

Action oriented theories of public administration are theories of social construction that have provided *possibilities* for new ways of thinking and doing public administration. And rethinking the value of the path we are on is a challenge in itself. Indeed, scholars have often felt that our administrative systems are not in touch with citizens, that the bureaucracies carry out their practices in a weakened or failing “electoral democratic accountability loop” that no longer serves a democratic society. “Citizens count” has been a theme that has carried on in the work of Cheryl King and Camilla Stivers (1998) and experiments in engaging citizens in urban settings can be identified (Berry, Potney and Thompson 1993) and collaboration with citizens is a central feature of such engagement (McSwite 1997; Fung and Wright 2003; Fung 2004). What emerges is a social construction (Jun 2006) that is based on pragmatism that is grounded in citizen engagement. And citizen engagements have different forms and involve various kinds of networks, each contextualized within their own environment. Public management theories that stress relationship-centered approaches, and policy and administrative theory that emphasizes the creation of shared meaning, and interdisciplinary approaches that provide new ways of thinking about public administration problems provide the focus for the action-oriented perspective.

To summarize, action-oriented perspectives provide possibilities and insights that engenders creativity in others, inspires them to think anew about what they see and has meaning. Such possibilities stimulate new advances in engaging citizens and administers toward a new approach to public

administration, such as those espoused by Janet and Robert Denhardt in their work, entitled, *The New Public Service* (2003).

Table 1 represents a summary of the three public service domains and the two fundamental perspectives as outlined in this essay with regard to public administration theory. Repeating the central theme stated earlier in this essay: *what* the researcher in public administration focuses upon (managerial and organizational processes or administrative and policy influences) and *how* they approach their subject (testing or developing theories) defines their goal of research and the relationship that research has with theoretical concerns.

*Table 1. Public Administration Domains and Perspectives*

	Positivist Perspectives	Action Perspectives
Public Management Theory	Science Method As a Tool of Inquiry	Relationship-Centered Approaches for Inquiry
Policy and Administrative Theory	Deduce Meaning	Created and Shared Meaning
Interdisciplinary Theories	Transferable Logics	Seeking Insight From Reframing Logics

## Summary

It is time to return to the questions addressed earlier in this essay. Namely, what do we mean by theory and what is the role of theory in the study of public administration? Do we need to include management processes and organizational contexts to improve public administration theory? Has theory excluded important practical leaning from the practice of management?

What this review indicates is that the theory “domains” of public administration are usefully informing the practitioner and the scholar. The difficulty is in how we are to



codify our knowledge development. Is each of the domains similar in the accumulation of knowledge?

In order to understand the role of theory in the study of public administration, it will be useful to embrace the following contributing parameters: (1) clarity in the purposes of research that is undertaken; (2) employing systematic inquiry; (3) recognizing the interdisciplinary roots of an inquiry; and (4) scanning the “domains” of theory for relevant insight to the research purpose.

### **Purpose of Research**

This research imperative can be placed into one of three purposes of public administration research: (a) theory testing, (b) evaluation, and (c) solution development. Thus, useful theoretical contributions can find homes based on these three purposes of research. With the first of these, theory testing, the research purpose is characteristic of traditional social science research. Each of the domains has various theoretical orientations that can contribute to the development of theory within the domains.

With the second of these purposes, evaluation, the research purpose is characteristic of both program and policy evaluation research. While classified within the domain of public policy in this essay, evaluation as a field may soon be treated as its own domain that will lead us to treat knowledge development within its own context. It is the evaluation area that implementation interests are best placed. Given the classification of this essay, public policy literature on program and policy evaluation has a great deal to contribute to the design, process and behavioral imperatives that are part of the evaluation/implementation processes. As such, we can confidently argue that we have a great deal to say about this domain as we have an accumulated body of knowledge.

With the third purpose, solution development, the research purpose is characteristic of both “private” and “public” management theory that seek to improve management information and practice. The contributing schools of thought include various management processes in the domain of administrative studies. Seeking applied solutions will involve model building but the focus on either utilitarian or socially constructed outcomes becomes paramount over any resultant “theory” which may evolve. Much like Koontz argued earlier, however, this area of study is not likely to easily generate knowledge accumulation, as will the other areas, in that experience drives understanding and there is a unique predisposition for those who study this area to stress the importance of contextual considerations that significantly differentiate settings and make simplified applications inappropriate.

Indeed, various disciplines (or fields of inquiry) have much to say about each of these purposes. *The use or application of theory, then, is dependent upon the individual who is involved in the public administration activity and their research preparation and purposes.* In short, a common, systematic and known boundary of public administration theory is not yet universally available. This is true despite various academic programs carving out their own public administration direction.

### *Systematic Inquiry*

In terms of theory development, one common element among this breadth and diversity in “domains” is that public administration research rests upon systematic inquiry. From a positivist perspective, all research must aim to be accumulative and as a result be based upon reliable methods of data gathering and systematic processes of observation and reporting. It is only through these criteria that we will be able to overcome the consequence

of diverse approaches to our subject matter. From an action perspective, meaningful policy and policy implementation will take place from a discourse with all participants and from the reflexivity and reflection on the part of public administration leadership.

### *Interdisciplinarity*

The boundaries of the public administration field must include interdisciplinary study and that the theories that inform the curriculum must come from various fields. While this approach is unsatisfactory to some in the field who are interested in developing a singular discipline of public administration, the efficacy of interdisciplinarity remains for both theory and practice considerations. Such an approach has some consequences that are difficult to live with, especially the outcome that it will be difficult to develop and accumulate knowledge. That is, without a common and unified agenda of research with regard to the unit of analysis, it will be difficult to build unified theory.

### **Scanning the Domains**

There is much to draw upon to inform Public Administration, and the field enjoys a rich tradition in borrowing theoretical work from various fields and exploring their use and relevant applications. What some have referred to as an “intellectual crisis” others see as a benefit. Perhaps such is the case because of the nature of the field. As noted by Richard Stillman, public administration is a very new field, only beginning to seriously mature in the early twentieth century in the United States and suffering from a contextual fear of an imposing state. As a result, we may be better at exploration than any of the other disciplines or fields of inquiry. However, given the highly fluid nature of social interactions, it is H. George Frederickson (1999) who argued that it is the field of public administration that is uniquely qualified to

offer new theoretical insight into the evolving networked field of governance, as it is public administration that studies “the adaptation of public institutions to high fragmentation” that characterizes the current environs of the state.

The key problems ahead for the study of public administration rest in these areas of study: what is the role of government? What is the role of the state? The function of theory will best be placed within this context as well as understanding the purpose the theory is to be used: theory-testing, theory development, evaluation and solution orientation. For management, do we focus on better practices or do we study the behavior of our subjects. We will likely continue to do both. And we should.

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## Public Choice Theory

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### **Introduction**

Traditional students of economics used to call their subject “political economy”. It was however primarily straightforward economics even though these students usually did have political ideas of one sort or another. Most of them, for example, were in favor of democracy, although sometimes a rather limited type of democracy. Ricardo in fact held a seat in the pre-reform Parliament. John Stuart Mill argued for the elimination of the rotten boroughs, but was not in favor of universal manhood suffrage.

Thus the term “political economy” really meant something much like “economics” today although the political economist of that day, like modern economists, normally had ideas about politics in general and government organization. Like conventional economists of today they seldom wrote about the latter topic.

There was however one area where the traditional economists provided a useful insight for public choice. This was in the economics of externalities. Largely in the 20th century economist began calling attention to the fact that private arrangements between citizens might affect the third parties. Thus a rowdy party may disturb the neighbors. More importantly, industrial activities frequently create negative effects on neighbors. The early writing frequently talked about smoke from a factory chimney, but there are many other examples.

### **Bargaining and Externalities**

At first glance it would appear that this problem could easily be dealt with by a bargain among the people concerned. Consider a smoking chimney produced by a factory with many houses nearby. This

inconveniences the householders, but abating the chimney would be very expensive for the factory owner. Of course, the factory owner could pay the householders for the damage is smoke inflicted or the householders could pay him to stop emitting the smoke. These would be private bargains, which at first glance need not to involve the government. The possibility of such bargains was first pointed out by Ronald Coase and his work, which won him a Nobel Prize, is usually referred to as the Coase theorem.

The problem is bargaining cost. If there are number of householders each one of them would make a profit by holding out for excessive payment for the smoke damage or if the idea is to pay the factory owner to stop emitting smoke, one of them could refuse to pay his fair share. This is a rather conventional bargaining problem, which arises whenever a considerable number of people have similar interest, but all of them would prefer to have someone else pay. It is usually referred to as the “hold out problem”.

Government, which can use compulsion, provides a solution to the problem. If the householders voted a smoke abatement law, the factory would have to conform. On the other hand, if the law required the factory owner to make a certain payment to each householder, that also would solve the problem. Thus the difficulty here is not entirely the externality, but the difficulty of bargaining for a solution. In a way we can say that most bargains in the market involve an externality of a very limited scope. It's not the usual way of describing the matter, but if I buy something from someone both of us gain and it can be said that the previous situation in which there was no bargain was an unusual form of externality. This is not the normal language, but considering it makes a little easier to understand the problem of the smoking chimney.

Thus government action normally described as eliminating an externality could as well be described as creating and enforcing a bargain between the parties. Normally, of course, there is little bargaining between the parties in making up the government-imposed solution. Normally the government simply coerces action and thus eliminates the externality.

Of course the action of government itself can be an externality. Roads are commonly, but not always, constructed using eminent domain to obtain the real estate. The householder or farmer who will find him self-losing part of his land to the government for a road may reasonably consider him self aggrieved. Rarely do people whose land has been taken under eminent domain feel fully satisfied with the price. The dissatisfaction can go either way. Perhaps the taxpayers feel that too much money has been spent on this particular piece of real estate. Further, as we will discuss later, the government frequently acts on the result of the internal bargaining within the government by the affected parties. This is called “log rolling”.

Early economist writing on the subject normally simply recommended some kind of government activity. They rarely considered the possibility that even a well-intentioned government might do the wrong thing. They also ignored the possibility that the government might create externalities itself. At the moment of writing the citizens of Iraq have learned that governments can create externalities, both negative and positive.

But war is not, of course, the only example. The author of this item frequently uses interstate 66. This is too narrow and at some times of the day badly congested. This clearly imposes externalities on me. The noise of the interstate traffic imposes externalities on people living along it. It is their political influence, together with that of some misguided environmentalists that

prevent it from being widened. There are in fact many other areas where governmental activity although beneficial for the immediate recipients, injures third parties. This is as much in need of remedy as the more traditional type of externalities. But, more of this later.

### **Clubs and Voting**

Interestingly, the question of how many people will be in a governmental unit also raises similar problems. This is normally discussed under the title “the theory of clubs” and the initial work was done by James Buchanan. Consider a very simple case in which a group of people would like to build and then use a swimming pool. The number of people who join the group is a significant variable. If there are too few they will not be able to afford the pool, or at least will have to pay excessive membership fees. If there are too many then the pool will be badly crowded. Thus each person entering the club generates an externality, which at first is a positive externality and then as the pool gets more and more members becomes a negative externality.

The same problem occurs with almost any government activity. There is an optimal number of members and hence a “club” externality. One solution for this is federalism in which different government activities are carried on at different levels. Those, which require large numbers of people, like war, can be done on national scale and many other activities can be done locally. Unfortunately it is rare that the activities are perfectly divided between different levels of government (Wrede 2004)

It would be nice if the problems were confined to voluntary swimming pool associations, but it also applies to governments.

The first significant work in which economics was applied to the political



structure itself was Duncan Black's initial work on voting. This was done actually during World War II and he sought publication almost immediately after. As result of a really horrible experience with referees, his work was not published until many years later. It does not appear to be much known to students in the field.

Kenneth Arrow had better luck with referees. His general impossibility theorem was written shortly after Black, but was accepted almost immediately and is still, after many years, occasionally cited. In it he showed that no voting method could meet a set of apparently elementary criteria. His work did not resemble that of Black at all except in the rather pessimistic conclusions for democracy. In his case the article, temporarily, became famous. Apparently, however, no one now takes either of these proofs seriously. Democracy remains highly popular among intellectuals and these two proofs have more or less gone into the memory hole. The author of this entry has written a long article on the subject, "Problems of Voting", and suggests that readers turn to that article (Tullock 2005) for further information.

### **Public Choice and Bureaucracy**

Leaving aside this mathematical work, which rather implies that democracy is either impossible or in any event quite different from its popular image; let me continue with a discussion of the work that has been done in public choice. There has been some work done, primarily by myself, on undemocratic government using public choice tools. The bulk of public choice, however, has dealt with democratic governments and to a lesser extent bureaucracies, mostly assumed subordinate to a democratic sovereign.

In general, public choice makes much the same assumptions about human beings and their behavior, as does economics. It is

assumed that they are mostly, not always but mostly, aiming to increase their own or their family's well being, not some badly defined public interest. The elected politicians are assumed to be much like businessman in that they select policies much like an automobile company selects designs of cars. The objective is to please the people who have some control over the actor's well being, for politicians the voters, and for manufacturers of automobiles, the potential customers.

The rest of the governmental apparatus is usually referred to as the bureaucracy. The bureaucrats are assumed in public choice to be ordinary people primarily interested in the compensation they receive for their work, although they may feel some satisfaction from promoting the public good by their activities. Whether they in fact always promote the public good is open to debate, but they probably think that they are doing so. There are, of course, some corrupt bureaucrats who are primarily interested in what they can make from bribes, but in the United States, and most advanced countries, this is a small minority.

Most bureaucracies developed internal patriotism. The personnel in any given bureaucracy tend to think that that particular bureaucracy is very important and probably should be expanded. Further they generally feel that the bureaucracy as a whole is important and should be expanded. Partly this is a matter of self-interest, a larger share per se will have more possibility of promotion. Further if more resources are put into the bureaucracy wages may be raised.

In all honesty, however, it must be admitted that such simple personal maximizing goals are not by any means the only reason why bureaucrats normally tend to favor expansion of their particular bureaucracy. In the first place, the bureaucracy and the particular part of that in which a given bureaucrats and is employed,

may well be contributing to the public good and its expansion might well be desirable in terms of that public good. Even if that is not true, in fact, the individual bureaucrat is apt to think that it is true simply because he has been working in the area for some time and has acquired a set of attitudes and beliefs consistent with the desirability of that bureau. Thus he can have a defensive attitude toward the bureau and indeed want to have expanded for the best of motives, even if an outsider might think his judgment is corrupted by his bureaucratic experience.

In most modern democracies, their grants are protected against being fired or demoted by their superiors by the civil-service regulations. This to some extent is made more important by the fact that bureaucrats can vote. Since they're many of them, they are politically powerful and can protect their privileges if elected officials wish to curtail them. In most modern governments, the bureaucracy has been expanded well beyond the optimal size.

### **Democracy and Elections**

In general, public choice has dealt only with democratic governments although the author of this item has written *Autocracy* (Tullock 1987) on non-democratic governments, and there is a small literature by other public choice scholars in this area. This item, however, will be devoted entirely to the democratic main corpus of the public choice literature.

Democracy means government by elected officials or, occasionally and mainly in small societies, by direct voting on the issues. This immediately raises the question of who can vote. Venice, which I think really should be listed as a democracy permitted only about 5 percent of the adult males resident in Venice to vote. At the other extreme, a tribe in New Guinea, which had been impressed by its contact with American military personnel in

World War II, permitted everyone over the age of 10 to vote. From the reports of the rare anthropologists who have visited the area, it worked out reasonably well.

More normally we have some intermediate level. At the time the United States adopted its constitution voting was restricted to white males who had a minimum amount of property. The franchise was gradually extended in the United States with the property requirements being early eliminated and women permitted to vote after 1919. Southern blacks were prevented from voting until the 1960s. In all of this United States was not too deviant. Women were in general not permitted to vote until the 20th century. Interestingly imperial Germany extended the franchise to women before United States, while England did not complete the enfranchisement of women until 1931. Until nearly the end of the 20th century women in the United States could vote as soon as they were 18 while men had to wait until they were 21. It is sometimes alleged that this was one of the reasons for the use of the draft.

Confining ourselves however to the kind of government which is elected democratically, rather than the direct democracy which is basically less common, one of the first discoveries of the early public choice scholars was that it is hard to explain why anyone votes. The likelihood of your vote changing the outcome except in very local elections is so small that it cannot provide the motive to vote. Public choice scholars sometimes say, truthfully, that you are more likely to be killed in auto accident on the way to the polls than to affect the outcome in a presidential election.

This problem has led to a good deal of investigation, but in view of the author of this item (who does not vote) it's hard to find a practical explanation. We are indoctrinated in school and there is a large-scale propaganda effort during elections. These may lead to

voting, but that is more a statement of emotional conditioning than of rational thought. In practice less than 50 percent of Americans who are eligible vote for Presidents. The turnout for lesser elections is smaller.

There is a rough rule of thumb, which is that voting is heavy when the democracy is first introduced and then falls off over time. This is however only a rough rule of thumb. Sweden and a few other countries have high voter turnouts even though they had been democracies for a longtime. Australia, a few Swiss cantons and a random sample of other places use legal compulsion to get people to vote. There is a good deal of social pressure exerted everywhere aimed at the same end. At election time there is also a good deal of propaganda by the candidates, which among other things, probably leads to more people voting than would without it.

In high school we are told that we should cast informed votes. In other words we should consider the whole matter seriously and at length. Apparently most voters disregard this good advice. Frequently campaign advertisements only tell the voter the name and office sought by a given candidate. It should of course be pointed out that candidates spend a good deal of time and energy preparing and giving speeches, which may have significant substantive content. They also sometimes circulate printed matter with substantive content. Nevertheless far more money is spent on one or two sentence television ads than on serious efforts to convince an informed voter.

### **Money and Politics**

This may be time to discuss the role of money in political campaigns in the United States. The view that large corporations make large gifts to campaign funds is fortunately or unfortunately false. A recent very careful study of the data on the subject shows that the

campaign finance is largely a matter of a large number of moderate, around a thousand dollar or less, contributions. Even the presidents of large corporations with incomes up in the millions make only rather small personal contributions. Their corporations, strictly speaking, make none because it's illegal, but some money does leak through the legal barriers. The large corporations and other interest groups spend about five times as much money on lobbying in Washington as on campaign contributions.

Money does, however, play a significant role in maintaining the current congressmen in office, but it is government money. Each congressman is provided by the government with a large staff, much of which is in his government provided office in Washington, but which also has a significant branch in his constituency. The staff devotes most of its time to helping the congressmen get reelected. Its existence is probably the main reason that congressmen so rarely are defeated in the elections. Indeed in the period before elections newspapers list "open" seats which are those where the incumbent is thought to be in danger. The number rarely much exceeds 20.

This is a radical change from the situation in the earlier part of the history of the American government. In most of the 19th-century congressmen served one or two terms. The apparent change to an almost lifetime career coincided with the provision of large office staffs, travel allowances, free postage and the ability to call on ordinary civil servants, now much more numerous than in a 19th-century, for assistance. It's not obvious whether this change is desirable or undesirable.

But it should be pointed out that the fact that the congressmen make their living by winning elections and have this large staff does not mean that the voter's desires do not affect the votes of the congressmen. The staff

has as one of its main duties keeping the congressmen well informed about the desires of the voters in his district, particularly those voters who are on his side. Whether spending all of this money on the staff which both helps congressmen in his efforts to get reelected and, as part of that, makes him well-informed on the wishes of his voters, is pro or anti-democratic is not obvious.

No other democracy has quite as much of this kind of government support for incumbents, but the political turnover in most of them is very small even if not as small as in the United States. It is sometimes said that the congressman's tenure lasts longer than that of the Lords before the recent reform.

### **Different Systems of Government**

So far this item has dealt mainly with American politics. Public choice was invented in the United States and although there are active foreign chapters to the Public Choice Society, its research has tended to concentrate on American politics. This is partly due to the fact that it's easier to proceed forward with work already done than to be a complete pioneer, and partly due to the fact that data on American politics are both more voluminous and better cataloged than in other countries.

Probably the most significant difference between the Anglo-Saxon system and the proportional representation system, which is followed by majority of countries in the world, is the weakness of party discipline in American legislatures although not in the English variant. This means the analyst can pay more attention to the individual politician and less to the parties. Nevertheless it is unfortunate that there is not more public choice research devoted to non-American parties. The amount is not, of course, zero and, indeed, in Switzerland there has been a good deal of excellent work, which pushes the general knowledge in the field forward.

Nevertheless for quite some time it was almost an American specialty, although this situation is rapidly changing.

Democratic governments are normally classified in two general systems, first past the post elections and proportional representation. There is a third method usually called the Hare method, which is complicated, and little used and hence will be omitted here. First Past the Post was the earlier form of democracy, used in England. The country is broken up into constituencies each of which sends one representative to the Legislature. As a general rule whichever candidate gets the largest number of votes is elected even if that number of votes is much below a majority.

Much the same method is used to select American presidents, although the electoral College makes a matter more complicated. One of the problems with first past the post is that with more than two candidates the winner may have less than a majority of the votes. Lincoln in his first election obtained only about 35% of the popular vote and probably could have been beaten by Douglas in a two-candidate election. Wilson in 1912 had more votes than either of his two opponents, but probably either one of them in a two candidate election could have beaten him. In England, since the 1920s, there have been three parties with the Liberal party receiving only roughly 10% of the votes. As a result the party that wins the election normally has only something like 45% of the popular vote. Arrangements for a run off between the two leading candidates are part of the system in some states, but sometimes lead to peculiar outcomes.

With legislatures elected by this method, party discipline is frequently weak. In United States Senators or representatives voting against their party are not at all uncommon. In England very strict restrictions on the campaigning of individual candidates for the

Legislature have led to an equally strict party discipline in the House of Commons. Of course the government itself is elected by the Commons rather than being independently elected as in governments which are copied after the American.

In most cases where proportional representation is used, the cabinet is elected by one of the two houses of the Legislature if there are two. Normally the house that elected cabinet is thought to be much most important. Sweden for example has abolished its second house. But even though the house, which elects the cabinet, is more important the other house may still have considerable power. The present situation in Germany is an example.

Normally, party discipline is quite strict in proportional representation governments. On the other hand it is very common for no single party to obtain a majority with the result that the government is a coalition among enough parties to get a majority in the Legislature. Usually discipline among the members of the Legislature within their parties is strong, but individual parties may deviate from the rest of their coalition partners. Normally this causes the government to fall and a new coalition must be made up.

The organization of the United States government with two separate branches of the Legislature enacted in radically different ways together with a President who, in essence, functions as a third branch is important. The President can veto any bill passed by the legislatures and they must have a two-thirds majority to overcome the veto. This differs from many foreign countries where there is a single chamber exercising dominance and frequently actually selecting the executive branch. It is thus much harder to enact new laws or increase government expenditures in the US. Probably as a result of this, the American government takes a

smaller share of GNP than most democratic governments.

## **Rent Seeking**

Here we must deviate to discuss rent seeking. This concept invented but not named, by the author of this item, is now found throughout the whole of conventional economics. It is however very important in public choice and hence a brief explanation here is necessary even if the reader is urged to turn to the separate item on the subject.

Briefly rent seeking originated in an error made by most economists. Creating monopoly causes two effects. Due to the higher price not so much of the product is sold and this creates what is called the welfare triangle effect. Conventional economists until recently, however, regarded this is the only social cost. The raising of the price on units actually sold, they argued, transferred money from the customer to the monopolist, but since they were both within the economy this was a transfer and not a social cost.

The problem with this is that it assumes that the creation of the monopoly or other special privilege does not involve the investment of resources. It's a free gift by society to people who on the whole are not regarded as particularly deserving. This is obviously an error and the author of this item is proud of being the first to catch it. There obviously are resources invested in creating monopolies or special privileges and there's no reason why the return on those resources in a competitive market should be higher than that on resources invested in more conventional ways. Retrospectively this seems obvious, but escaped the attention of economists for a very long time.

At the moment of writing the Bush administration is considering either abolishing or at least cutting the tariff on steel. The steel industry and in particular the

steel workers are engaged in a very vigorous and expensive campaign to stop these cuts. Surely the cost of this campaign should be included as a social cost of the tariff itself. The earlier habit of ignoring this was clearly in error.

### **Public Works and Logrolling**

This is a correction in the standard theory of the market, but also very important in public choice analysis of politics. It is not only tariffs or adjusting tax rates, but there are also questions of what public works shall be built and where they shall be built. The first article in which the issue was raised, long ago, dealt with road repairing and involved what is called log rolling which means essentially that politicians trade projects which will benefit one particular set of politicians for another benefiting another set. Even if public works are frequently very valuable this kind of local interest tends to lead to over investment. One who looks over the expenditures on projects by almost any government, will quickly find cases where either the project should not been carried out at all or where it is much larger than it should be.

I usually use the central Arizona canal project, the Tulsa deepwater port, and ethanol as my examples. This is, however, merely my personal set. I'm sure the reader can quickly think of another collection of wasteful projects. What happens is that the congressman from, let us say, Arizona, votes for the Tulsa deepwater port and ethanol in return for congressmen from districts benefited by those voting for the central Arizona project.

It should be pointed out that logrolling can, on occasion, prevent desirable projects as well as creating undesirable ones. The environmentalists feel strongly and rarely engage in careful calculations. Thus by logrolling, they can prevent desirable

investment sometimes. This is, of course, only sometimes. Many times the environmentalists by preventing projects from being carried through create a public good or prevent a public bad.

Desirable projects frequently involve log rolling also. Usually at least somebody is injured and should be compensated. When nobody is injured some congressman may nevertheless insist on being compensated for their favorable vote by something for their district. But we would like to have log rolling only for those projects with a net effect positive.

Logrolling would be highly desirable if the voters were well informed. Consider a set of road repair projects to each of which is worth more to the people who directly benefit than to the taxpayers taken as a whole. If everyone simply voted in accordance with their own interests, all of these projects would fail. A bargain in which all of the projects would be implemented and paid for by all of the taxpayers would clearly be in a public interest. A lesser program in which 51 percent of the roads were repaired by taxes falling on the entire population would attract majority of the votes, but whether it would be thought to be in the public interest is questionable.

More often than not, there is negotiation in which the people who will benefit from one project, for simplicity assume repairing one road, bargain with other small groups of people each of which has a somewhat similar need for a particular government expenditure and are willing to pay at least something for it. Note, however, that is only necessary to get a majority of the people voting for your project so you need only to make bargains with half of the other voters. Since you'll end up paying for only half of the cost of the projects, you should favor much more road repairing than you would if you had to pay for the whole of it.

If, for example, the Constitution were changed so as to require two-thirds vote to pass a bill the over expenditure would be less. This is, however, a possible but highly controversial proposal. Indeed it is one of the areas where public choice scholars normally find themselves disagreeing with the average intellectual. In any event it merely reduces the over expenditure. Unanimity, which would eliminate it, is normally thought to be immensely impractical.

The consequence of this is large-scale misallocation funds for government. Logrolling bargains normally are not confined to a single topic such as roads. Widening one road at the taxpayer's expense may be part of a bargain, which includes keeping a military base open, a tariff on steel, and a pay raise for teachers. Further, the politicians rarely make careful cost benefit calculations so the outcome may be highly inefficient.

Note that all of this requires considerable ignorance on the part of the voters. The voter who votes for Congressman Smith because he was active in getting the road widened probably does not even know of the bargains on steel or the military base. I recently attended a large reception to which a state senator was also invited. They have a large poster up in which his picture appeared together with the slogan "He gets things done." No doubt he did, but probably the voters would be better off if some of them have not been done. As a result of this phenomenon, voters' calculations are normally pretty bad.

### **Information and Democracy**

One way of dealing with this problem would be to increase the voter's information. I don't think any serious student of the problem gives this particular solution much thought. Every effort to find out what the voters know invariably turns up extreme ignorance. Except

at election time most voters probably cannot recall even the name of their congressman let alone his complete voting record in the last session. Further although he may make an effort to persuade them to vote for him he is unlikely to provide them with detailed information about what he has done and what he proposes. Promising specific benefits without specifying what other projects he will vote for in trade to another congressman for his projects is the normal rule.

This could be taken as an attack on democracy but in order to reach that conclusion the critic must have a better system in mind. Normally he does not. This kind of trade is found everywhere in democracies, but also in other forms of government. Insofar as it is less carefully concealed in democracies than in monarchies it's actually an argument for democracy. Nevertheless it does lead to considerable inefficiency in government. Once again, critics should attempt to produce a better method rather than simply say that this method is far from Divine Wisdom.

This leads to what is probably the most controversial proposal in public choice. With simple majority vote many things get through which would not get through if you required a reinforced majority. Of course any believer in Paretianism would favor unanimity which guarantees that no one will be hurt but also probably guarantees that very little will be done. A two-thirds or 3/4 majority would rule out many undesirable projects and not so many desirable ones.

If we consider what actually goes on in the American government, simple majorities are by no means universal. Juries are required to be unanimous, and amendment of the Constitution requires much more than a simple majority. There is the already mentioned Presidential veto and a two-thirds vote in both houses requirement for overcoming it. Just at the moment the Senate

is requiring a 60 percent vote for various matters. Interestingly, it is the conservatives who object to this and liberals who are in favor of it.

With a two house Legislature where each house is elected by somewhat different electorates, it is likely that a majority in both houses represents more than half of the voters. The Presidential veto raises the voter support required even further. Thus a proposal for more than simple majority is far from revolutionary. Nevertheless it should be said that this is the one aspect of public choice theory, which has met with the most objection. The early public choice proposal that any constitution should be adopted not by a reinforced majority, but by unanimity is in practice supported by almost no one. Fortunately quarrels over this particular aspect of the theory have not so far impeded progress in the general field of public choice.

### **Bureaucracy**

Let us now turn to the bureaucracy. The first thing to note is that bureaucrats are much like everyone else. They're interested in their pay, their work, and prospects of advancement. They're usually also interested in trying to help the world by their activities. But like the private citizen employed in, shall we say, a steel mill, they really don't modify their activities very much to create a benefit for the public interest. It is true that they frequently say that they are motivated primarily by a desire to help the country. This is not by any means entirely hypocritical. Like everyone else, they do have good intentions, but their behavior is seldom dominated by them except in those rare cases where improper behavior might lead to catastrophe.

Most people tend to convince themselves that whatever they're doing is not simply a way of making a living, but also has public good attached to it. Bureaucrats are in a particularly good position to feel this way and

usually do. They may well have developed a sort of departmental patriotism in which they feel that expansion of their particular bureau is an accord with a good, the true, and the beautiful. Thus they have morally correct arguments for expanding it or at least not shrinking it

These are reinforced, of course, by personal ambition. If the Army is expanded there can be more generals. In the American federal bureaucracy, this motive is not strong because transfer from one branch of the bureaucracy to another is easy. General proposals for economies, however, are usually objected to by all the bureaucrats. The fact that there are many bureaucrats and they mainly vote means that Congress must take careful attention to their desires. It is very close to impossible to fire federal bureaucrats and a general proposal for major reductions would almost certainly not get through Congress except under exceptional conditions.

Speaking as a former member of the Department of State bureaucracy, I have a low assessment of the efficiency of the whole apparatus, but that may be generalizing my own experience to a more extensive organization. Certainly a large organization is necessary to carry out the many duties of modern governments. It seems likely, however, that we could get by with smaller government. In fact ours is smaller as a share of GNP than most European governments and in my opinion this is fortunate.

### **Conclusion**

We've now finished our brief survey of the new field of public choice. Discussion of governments has traditionally turned largely on ethical and public good aspects. There is no doubt these exist, but the more earthy aspects of government are also important. As a matter of fact public choice has only begun its research into government and has so far



had very little effect in making improvements. I can only suggest that we should work harder and be more persuasive in urging reforms. The effort (we hope) availeth.

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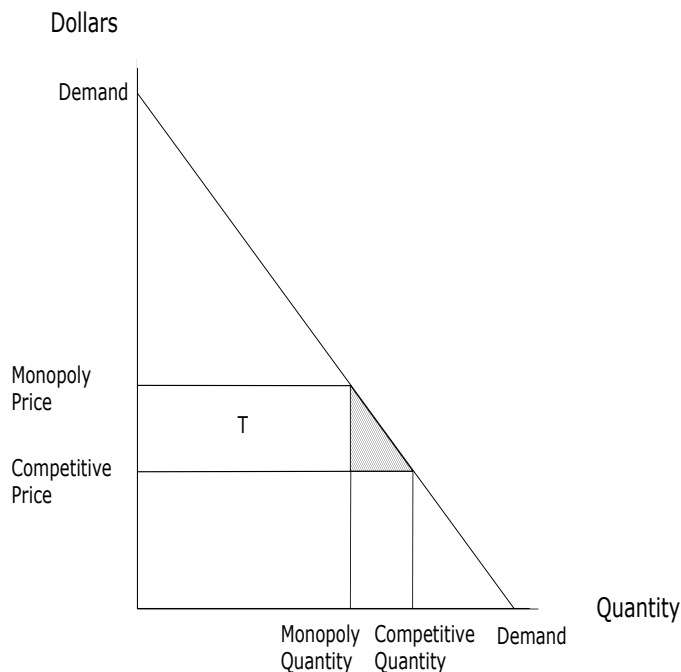
## Rent Seeking

*Gordon Tullock*

### Introduction

The subject of this particular item in the encyclopedia is a relatively new field of economics, which was, rather by accident, started by the author. Thus in a way it will combine a discussion of economic theory with some autobiographical notes. It may also be encouraging to the young scholars just starting out. It will report on one of the most important articles in economics being turned down repeatedly and eventually getting published so obscurely that the basic idea was reinvented by another scholar.

Traditional economics in discussing tariffs and monopolies had a very serious error. Figure 1, below, was the normal illustration used for both of these items, but it was misunderstood.



It shows the quantity and price of some good on the two axes. The line CP shows a competitive price and the line MP the price under monopoly or if foreign goods are kept out by a tariff.

The error is from assuming that the social cost is the shaded triangle. This is, of course,

the cost inflicted on the community by the fact that people who would like to buy the good at price CP cannot do so. Clearly it is a social cost, but what about the rectangle to the left. The traditional argument here was that this was merely a transfer since both the people who paid this additional price and the monopolists who received it were members of the community and hence the total amount did not reflect a true social cost.

This position, which today seems absurd, was held by substantially all the authorities and appeared in all the texts. Further it seems to have been firmly engraved in the minds of all economists since, as will be explained below, a number of leading journals rejected suggestions to change it.

There were some numbers available, mainly computed by Harberger (1954), which showed the welfare cost of tariffs and monopolies in several nations. This was, of course, the orthodox triangle with the rectangle left out. His results were, I think, quite surprising to most economists. Certainly they were surprising to me. They showed the total cost of protective tariffs and monopolies as of trivial importance.

This naturally raised the problem of why we spent so much time on the matter in economics courses and in the economic literature. Although Harberger raised this question, he made no effort to answer it. As far as I can see his attitude was the same as all of the other economists except the author of this item.

### The Source of Monopoly Profits

There is an obvious problem with this traditional solution, how do the monopolists or beneficiaries of the tariff get these large profits without apparently investing any resources at all? A steel mill worried about Korean competition would certainly not invest money in buying new machinery when for free they could get a tariff and drive the

price of the Korean steel in the United States up to whatever level they desired. This is absurd.

There is also the problem of purely domestic monopolies, assuming that they have no real social cost except the tiny triangle, why do we waste so much time on them. We might, of course, simply object to monopolists being wealthy, but that's a distributional matter and economists put them in a separate category from efficiency or inefficiency.

The answer to this problem, which I suggested in my first article, is simply that it assumes that one gets a tariff or a monopoly freely, as a gift of God. There is also the fact that not all industries are monopolized. If creating monopolies were a zero resource activity, we would anticipate that all industries would be monopolistic.

The solution to this is simply that it is not free to get a protective tariff or a monopoly. At the time of writing the question of whether we shall or shall not continue to have tariff on steel is upsetting not only the American government but a number of foreign governments. Further steel industry businesses and, in particular, steelworkers unions are spending a great deal of money on advertising intended to retain the tariff. Surely these expenses should appear somewhere on the figure and the logical place is, of course, in the rectangle.

Unless we believe that the activity of creating a monopoly or lobbying through a tariff is a remarkably inexpensive way of obtaining profits, we are stuck with the view that only the shaded triangle is important. Since the measurements mentioned above indicate that the cost is trivial, then the problem of monopolies and tariffs is also trivial. Although there was little or no progress until the author of this item's first article on the subject, economics professors

continued to devote a great deal of energy to denouncing tariffs and monopolies.

The solution here is simple. There is no reason why resources invested in trying to get a monopoly or a tariff should have a higher return per dollar invested than those put into other kinds of enterprise. Thus the total cost of monopolies or tariffs is the full area of the rectangle and the triangle. Those economists, and I regret to say that I was one of them, who taught that the rectangle was a transfer and hence not a social cost were simply wrong. Further, retrospectively, it looks like a particularly foolish error.

### **Emergence of the Rent Seeking Literature**

The author of this item was the first person who suggested that the traditional theory was simply wrong and that the rectangle was part, indeed the main part, of the social cost of tariffs and monopolies. I sent the article to the *Journal of Political Economy*, which promptly rejected it as did the *American Economic Review* which I then sent it to. I went down a step and sent it to the *Southern Economic Journal*, which also rejected. At this time I received a letter from the new editor of the *Western Economic Journal*, at that time a very minor journal, asking if I would send them an article. I sent it again and immediately received a very enthusiastic reply.

There was no response to this article which, granted the then obscurity of the journal, is not surprising. It occurred to me that straightforward income transfers raised the same problem and I made up a paper on this, which I read at a Swiss University. The editor of *Kyklos* was at the lecture and asked if he could publish the article, which I naturally agreed to. *Kyklos* is not an obscure journal, but few Americans read it.

At this point Ann Kreuger, who had not seen either of my articles on the subject, published a pair of articles in the *Journal of*

*Political Economy* and the *American Economic Review*, which basically made the same point that I had. She did not however claim any general application of her theory. All she said was that there was a special type of economy, the “rent seeking society”, in which resources were invested to obtain special privileges from government. The two economies she talked about were India and Turkey and special privileges mainly had to do with foreign exchange certificates, something which was unknown in United States. To repeat, she made no claim that the same problem existed in United States or other Western countries. But other economists promptly made the connection and her name “rent seeking” was universally adopted.

It's possible the Asia does have some effect in this area, but I suspect that it has more effect on the economists who are confronted with unusual circumstances in Asia. I myself had spent considerable time in China and Korea and that may have been one of the reasons that I saw the problem. Certainly there was great deal of “rent seeking” there.

Note that the journals, which turned down my article, accepted hers. They are a good pair of articles, but then my article was also good, which is demonstrated by the number of times that it has been reprinted. Indeed my article was much more general than hers since I did not say or imply that it required a special type of society or that it was confined to foreign exchange certificates.

Why then was hers accepted and mine not? I think the explanation was simply that my article was an implicit attack on all economists who taught their students the conventional wisdom. Ann avoided this by talking about an exotic custom in exotic places. She didn't, even by implication, attack the standard economic theory and those standard economists who had taught it. At the

moment which she brought it to the attention of a wider audience, however, it became possible to reprint my original article, and collect a number of other articles which were inspired by it after Ann's article had been published. In a way, her article, which except for its very narrow scope was identical with mine, opened the way for a great efflorescence of research in this area.

### **Special Interest Groups**

But granted that various types of special privilege and monopoly are not produced without cost for their beneficiaries, where are the costs and can we do anything about them? In some cases it is a matter of deliberate policy to confer a monopoly on the originator because we feel the social benefit of encouraging new inventions and production of literary works more than compensates for the monopoly cost.

At the moment a number of people involved with the Internet are investing very considerable resources in legal efforts to claim patent and copyright for their product. It's not obvious here that the extension, in providing motivation for new and expensive programs is worthwhile. In any event the turning to the courts instead of Congress for the extension is in a way an invention in itself. In this case it seems likely that the principal gain will go to the lawyers and not to their employers.

But turning to the more normal kind of rent seeking, there are the monopolies in private industry. We don't actually know very much about the activities of creating such monopoly because it has been illegal for most of the 20th century and hence there is little data. In the latter part of the 19th-century creating “ trusts” was a standard form of enterprise with Morgan making vast amounts of money out of it. It would be nice to have a good study of how resources were spent in those days to create monopolies, but so far as

I know the data does not now exist. Today private enterprise monopolies are sometimes created but it is done in secret because it is illegal. Hence we have no data on the actual cost.

Monopolies of labor, called unions, are perfectly legal and it would be possible to collect data on how much it costs to organize them. The switch to something close to a free trade internationally has, however, greatly weakened the unions. They depend in order to get high salaries for their members on the ability to raise the price of the final product. The Koreans and the Japanese ended that, although as mentioned above there is still rent seeking activity connected with an attempt to reinstall the tariffs on steel. Once again I do not know of any data on the actual cost of organizing unions.

But these are examples of rent seeking through the use of private instrumentalities. This is both much more difficult and much less successful than the use of the government for this purpose. To take an outstanding example, all over the developed world farmers have succeeded in getting government creation of monopolies and cartels for their products. Interestingly in the more poverty second parts the world the government normally engages in attempting to get the price of food down for benefit of the city dwellers who are politically more influential than the farmers in these countries.

But farmers are a small minority in most of the countries in which the government creates cartels to raise their price. They're less than 2 percent of the American labor force and similarly minor in voting power in such countries as Japan Korea and the European Union where the extortionate activities of the farmers are even more severe than in United States. How then do they acquire the political power to take so much money away from the average citizen by raising the price of his food? The dairy lobby is particularly

interesting in this case because it raises the price of milk, mainly consumed by babies and children. The total number of dairy farmers who support the lobby is quite small and in general they are very prosperous businessman. A modern dairy is quite a sizeable capital investment.

But if the extortionate increase in the price of food is the most common and conspicuous example of rent seeking, most government programs involve at least some. A new bridge, a tariff, a research laboratory in beekeeping located in some Congressman's constituency, or even a purchase of military aircraft from a company which regularly supports Congress or at least a congressman are all examples of rent seeking.

Note, however, that not all of these are wasteful. While the location of the bee keeping laboratory has been established by rent seeking, it is by no means obvious that it will not pay its way by improving our supply of honey. Roads are important and although they could be built privately and funded by tolls, that is not the route we have taken.

My favorite example of wildly wasteful rent seeking activity is the central Arizona project which is a canal collecting water from Colorado River and taking it all the way across the state of Arizona to Tucson, dropping of bits and pieces here and there for other cities and for irrigating crops which will later be purchased by the federal government in order to keep the price up.

We now turn to a very old and well-established custom of all democratic legislatures, *logrolling*. A congressman who wants something for his district, let us say a canal to deliver water to a major city in it, will realize that he cannot put it through by himself. There are only a very few other congressman who will benefit from this particular canal. He therefore looks around for other congressmen who want specialized advantages for their particular district and are

willing to make a trade.

For simplicity let us make use of a very simple model that I used in my first article on the subject, which was also my first publication in the *Journal of political Economy*. I assumed a large number of farmers living on a number of short roads which normally had about five farmers on each one and which connected to a major road running through the area. Repairing any given short stub road would benefit the farmers on it greatly and have some slight advantage to other farmers who might occasionally use it. The farmers being members of a democratic polity wanted to have the central government repair their roads but a petition from the farmers on a single road would probably not be successful.

### **Role of Legislature**

Under the circumstances the farmers, or their representatives in the Legislature, would make an arrangement with the farmers on another road. Suppose there are 100 roads and if the farmers on 51 of them vote to repair their roads that will be enough votes to get it through the Legislature. Assume that it costs \$1000 to repair each road, then this project for 51 roads will cost \$51,000 and the farmers on those roads would benefit. The tax however would fall on all of the farmers not just the farmers who live on those particular roads, but they would pay only 51% of the cost of the repair and would probably favor over repair of the road.

There two problems with this. Firstly, taken by itself, this is not an efficient allocation of road repair resources. Further one can assume that the farmers along the 49 roads that are not repaired will be unhappy. They can however make a deal among themselves and a few of the farmers on the roads that have been repaired to get their roads repaired too. This will require that the farmers on the roads were the two projects

overlap receives special advantages. The end product of this set of bargains is that all the roads are repaired to an excessive amount. For each farm road the cost of repair falling on the people who actually vote for that repair is only 51% of the total cost. That they choose a level of repair, which is excessive, is not surprising.

This is a very simple model, but more complex behavior of the same sort dominates most legislative bodies. It should be said that it does not necessarily lead to over expenditure on government projects because similar log rolling bargains maybe used to provide special tax exemptions for special groups. What it does mean is that there is no careful calculation on a project-by-project basis of the cost and benefits of these projects. Needless to say these roads are only a simplified example of what actually goes on. Tulsa is now a deepwater port because it's congressman made bargains with other congressman from places like Tucson which wanted water brought all away across the state of Arizona from the Colorado River in order to use it to spray their lawns. There is also, of course, the farm program in which mothers wishing to buy milk for their babies find themselves paying a price which includes a significant monopoly profit arranged by congressman who have enacted what amounts to a government run cartel for the dairy industry.

All this is in many ways a significant criticism of the way in which legislatures work. If the reader can think of a simple solution I think he should make it public. For myself, I realize that this is an intrinsic difficulty in democratic government, but I'm aware of other intrinsic difficulties in other forms of government. I would like to make some arrangement under which log all rolling was permitted of those cases where there are special advantages to a group of voters from government action, and the advantages are

greater than the cost while in those cases in which the cost is greater than the benefit to the society as a whole although the particular voters in the bargain make net gains would be prevented. But to repeat I can think of no way of doing this. All together, democracy does have disadvantages, but keep in mind that other forms of government have more.

## Conclusion

In general, rent seeking is characteristic of democracy and trades within the Legislature are equally characteristic. Rent seeking however is to be found in all forms of government and trades among the courtiers a royal court may be much more expensive than legislative log rolling in a democracy. Even if it isn't perfect, the representatives in the Legislature are under the control the voters, which we think is in general, in spite of all the defects, better than being under the control of a dictator or a King.

These things get through because the average voter does not know about the projects which are used by his congressman to get the benefit for the congressman's own constituency. Once again, however, these are not necessarily entirely wasteful. While the federal government was digging the central Arizona canal for the benefit of Tucson and other cities, it was also widening and improving the interstate, which ran along the edge of Tucson. Judging by the amount of traffic carried I think this would easily meet any cost benefit calculation, although I must admit that I have not seen the actual work of the economists and engineers on this project. Thus rent seeking, on occasion, may actually be the benefit of the general society.

While dealing with the cost of rent seeking one should take into account the amount of time spent by congressman in organizing the bargains. They have, of course, a sizable taxpayer funded bureaucracy in the form of their staff, which is a system for this purpose.

Further one of the costs undoubtedly is the cultivation of ignorance on the part of the voter. If these project did not tend to take up his time he might, repeat might, put more time into considering projects producing public benefit.

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## Small Nation Viability

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### **Introduction**

The viability of small nations refers to the environmental, social, and economic sustainability of small nations. Environmental sustainability depends upon the adaptability to climate change, the capacity to mitigate natural disasters, the efficiency of waste management, and the development of renewable energy resources. Social sustainability depends upon the adaptability to globalization and trade liberalization in terms of cultural norms and social cohesion. Economic sustainability depends upon macroeconomic adaptability, the capacity to attract foreign investments and to establish a proactive relationship between multinational corporations and domestic firms, and the capacity to develop areas of comparative advantage in global markets.

In all cases, sustainability ultimately builds upon the human capacity to niche expansion in societal evolution. As Boulding (1978) argues, humans create niches into which they expand, as they use knowledge, energy, and materials to produce the human artifacts of knowledge, technology, and organization, where increases in knowledge push back the limits set by energy and materials. Small nations may constrain the human capacity to niche expansion through knowledge growth, because of their smallness. The knowledge stock increases with population size and growth, as more people implies more knowledge and learning, and greater productivity, while the resource problems that arise may be resolved through innovation in a free society that allows imagination to flourish (Simon 1996). Small nations seem to have a disadvantage in knowledge growth, but a cluster of small

nations may have an advantage to a large nation.

When explaining the rise of the arts and the sciences, David Hume (1777) stresses that a free government is crucial and that the divisions into small states are favorable to learning by stopping the progress of authority and power, thus favoring a number of neighboring and independent states connected together by commerce and policy. Regionally integrated, independent small states will stimulate greater intellectual diversity, based upon persuasion and influence. Their position will be based upon what Boulding (1978) calls integrative power. This is the power emerging from role power based upon images in human minds; symbolic power that gives structures to roles; community power that creates benefits from membership; and moral power that arises when actual practices are perceived to be inconsistent with moral ideals.

Small nations constitute a heterogeneous group and can be defined in terms of population size. Armstrong and Read (2002) use a population of less than three million as criterion, which is smaller than mainstream economics defines as a small open economy. Their data set consists of a diverse group of small countries, including Barbados, Botswana, Cape Verde, Comoros, Guinea Bissau, Iceland, Jamaica, Kuwait, Malta, Mauritius, Singapore, and Tonga, among others. They find that the growth performance of small nations is positively affected by vulnerability when trade openness has a 50 percent weight, thus more than outweighing the negative effect of remoteness, and environmental vulnerability. Easterly and Kraay (2000) use a population of less than one million and find that small nations have higher per capita income levels and more volatile gross domestic product (GDP) per capita growth rates due to greater trade openness, but that the negative effects caused

by this volatility are more than outweighed by the positive effects of trade openness.

A definition based upon shared political interests led to the formation of the Alliance of Small Island States (AOSIS). As a coalition of small island and low-lying coastal countries that share similar development challenges and concerns about their vulnerability to adverse effects of global climate change, AOSIS with its 43 members and observers in Africa, Caribbean, Indian Ocean, Mediterranean, Pacific, and South China Sea works through the United Nations (UN) system (AOSIS, 2006). Its membership excludes some small non-island developing states, such as Botswana, Kuwait, and Swaziland, as well as small developed countries, such as Iceland, but includes other countries in the Caribbean, such as Cuba and the Dominican Republic. Nevertheless, most AOSIS members and observers belong to Armstrong and Read's (2002) data set of countries with a population less than three million. Singapore, which economically is a high-performing nation, provides a case in point, but the Singaporean view of trade openness differs from the one of small island developing states in general.

### **Sustainable Development of Small Island Developing States**

The small island developing states (SIDS) favor a holistic and integrated approach to sustainable development that takes into account economic, social, and environmental aspects that focus on what they perceive to be uniquely disproportionate vulnerabilities (AOSIS 2004). They point out the need for their greater involvement in international financial decision-making processes and institutions, but they also stress the importance of culture, the integral role of youth, and gender equality. As blueprint the SIDS refer to the Barbados Program of Action—Program of Action for the

Sustainable Development of Small Island Developing States, adopted by the Global Conference on the Sustainable Development of Small Island Developing States in Barbados in 1994—that presents a basis for action in fourteen agreed priority areas. These areas include climate change and sea-levels; natural and environmental disasters; management of wastes; coastal and marine resources; freshwater, land, energy, and biodiversity resources; tourism; national institutions; administrative capacity; regional institutions; technical cooperation; transport and communication; science and technology; plus human resource development (UN 1994).

Sea-levels, cyclones, volcanic eruptions, and earthquakes can have had extremely damaging effects on the SIDS. Land being very scarce puts greater demand on waste management and efficient land use, thus constraining tourism, while biodiversity is very fragile. These resource scarcities lead to the need for human imagination together with skills that Simon (1996) considers the ultimate resource in a free society. The Barbados Program of Action recognizes human resources as the most valuable asset of the SIDS. It also argues that effective human resource development in the SIDS requires greater attention to population issues, education and training, and health, including better health and social services, nutrition, housing, and female participation in development (UN 1994).

While the economic growth success of Singapore can be attributed to its location and city status, the economic growth success of Mauritius—a small island state very remote from international markets—cannot be accounted for by these explanations (Armstrong & Read 2002). Simon (1996) attributes the economic miracle of Mauritius to the adoption of economic freedom, and uses Hong Kong to illustrate that a high

population density together with a lack of natural resources is not an obstacle to economic progress in a free economy. Similarly, Bauer (2000) argues that economic performance depends upon personal, cultural, and political factors, on people's aptitudes, attitudes, motivations, and social and political institutions. He points out that sustained prosperity owes little or nothing to natural resources, as Singapore and Hong Kong illustrate. Hence, the problem of inadequate natural resources in the SIDS may be resolved by suitable cultural resources. The Mauritius Strategy was developed by the International Meeting to Review the Implementation of the Program of Action for the Sustainable Development of Small Island Developing States in Mauritius in 2005. It stresses the importance of culture, in particular the comparative advantage of the SIDS in the cultural industries, the importance of the cultural heritage, and the marketing of cultural products (UN 2005).

Bauer (2000) argues the outstanding lesson of Hong Kong is the role of personal aptitudes, motivations, social mores, and appropriate political arrangements. These are seen as being more crucial than access to markets. The SIDS see problems with trade liberalization, including severe impacts on their fragile economies and societies. Yet they aim for a greater role within the World Trade Organization (WTO) to maintain and create non-reciprocal preferences, and to compensate SIDS for their inherent structural disadvantages (AOSIS 2004).

The Mauritius Strategy, following up the Barbados Program of Action, posits that the SIDS face difficulties integrating into the global economy due to smallness, structural disadvantages and vulnerabilities. Not all the SIDS have a capacity to benefit from free trade (UN 2005). Assistance to upgrade capacities to enhance competitiveness of the SIDS as well as special treatment of them in

the multilateral trading system compensating for their lack of competitiveness were asked for. The latter would weaken the market process by preventing market prices from performing their function of conveying information, thus decreasing learning to the detriment of the economic calculation of domestic entrepreneurs. Furthermore, concerns were raised about foreign ownership of land, thus excluding local communities from land ownership. The perceptions of international trade and foreign direct investment seem to reflect a zero-sum game view of exchange.

Interestingly, cultural resources were acknowledged and cultural industries were seen as a means to nurture social cohesion and reinforce national identity, including civil society for sustainable heritage development. In addition, civil society involvement in the formulation and implementation of public policy was seen as essential to resilience building of the SIDS. The virtuous free-market economy of economic personalism underlines the crucial role of the small-group order of civil society. The moral and cultural institutions of society induce the free market to be a moral instrument for human development, because it achieves self-realization by entering into genuine community, while the small-group order creates a distinction between self-interest and selfishness (Santelli *et al* 2002). Civil society gives what Heyne (1985) calls the personal elements upon which rule-coordinated capitalist societies are founded. Integrative structures, based upon group identification that emerges out of individual images of personal identity and identity of others, are crucial to exchange, because exchange requires a small amount of benevolence (Boulding 1978). Civilization evolves spontaneously through submission to new rules of conduct, and the coordination of division of labor through market prices

requires diffusion of certain gradually evolved moral beliefs (Hayek 1979). Hence, the market is constrained by the moral culture of society rather than by the state.

Using Adam Smith's (1759) notion of fellow feeling, Rizvi (2002) makes clear that sympathetic normative understanding is quite possible, while Sugden (2005) points out that interpersonal relations endow corresponding sentiments, which are crucial to morality, with normative status. Cooperation between entrepreneurs in the Baltic Sea Area in the form of Baltic-Nordic learning networks may improve their global competitiveness, but requires a shared morality of markets that in turn requires civil society formation in the Baltic countries (Marmefelt 2007). Consequently, in order to improve their global competitiveness, the SIDS need to have strong civil societies that yield a shared morality of markets among them. In the AOSIS Strategy, the SIDS outlines a more integrated approach to sustainable capacity development, including civil society and combining features, such as improved domestic science and technology, human resources, and capacity of civil society to fully contribute to sustainable development (AOSIS 2004).

### **Global Competitiveness of Small Nations: Is Smallness a Disadvantage?**

The alleged disadvantages of small nations are not supported by empirical evidence. Easterly and Kraay (2000) study a large cross section of 157 countries, including 33 small states with an average population during the 1960-1995 period of less than one million. They find that if they control for the location by continent, whether they are oil producers, and whether they belong to the Organization for Economic Cooperation and Development (OECD), the small states are richer with better quality of life, and that their productivity advantage accounts for about

two-thirds of their income per capita advantage. The small states also benefit from greater trade openness, although it gives a greater volatility in real GDP per capita growth rates.

Armstrong and Read (2002) study growth performance and vulnerability for 93 states, out of which 38 are small states that satisfy the three million threshold during the 1980-1993 period. They use Briguglio's (1995) vulnerability index, which uses measurable proxy variables: exposure to foreign conditions (the ratio of trade to GDP), insularity and remoteness (the ratio of transport and freight costs to exports), and proneness to natural disasters (the economic costs of such events), weighted in the proportions 50:40:10, respectively. Armstrong and Read find that the SIDS tend to be more vulnerable than other developing countries and than other countries in general, and that there appears to be some positive correlation between their vulnerability, levels of GDP per capita, and Human Development Index (HDI), their higher HDI suggesting that they generate relatively more social capital. However, Armstrong and Read's most important result is that vulnerability has a significant positive effect on gross national product (GNP) per capita growth. Hence, they argue that this suggests that the vulnerability measure is swamped by the positive effects of the gains from trade and export-led growth. That is, the positive growth effects of trade openness more than outweigh the negative effects of remoteness and environmental shocks. They also point out that social cohesion is greater in small states. Hence, smallness may not be a disadvantage at all.

### **Global Competitiveness of Small Nations: Mauritius and Singapore**

Historically specific cases, such as the small nation success stories of Mauritius and Singapore provide some important lessons

that, if learned by other small nations, would contribute to the viability of small nations in general.

In Africa, Söderbom and Teal (2003) find that Botswana and Mauritius were the most successful in export growth during the 1970-1999 period: starting from approximately the same level of exports per capita in the 1970s, Mauritius exported more than four times as much and Botswana twice as much, while South Africa exported virtually the same, and Zambia less than one-fifth by the end of the 1990s. Both Mauritius and Botswana are small nations in terms of population, while Mauritius also belongs to the SIDS.

According to Bräutigam (1997), Mauritius is a small, ethnically heterogeneous island nation, whose shared ideology combines Fabian socialism and export-led growth as a development model. In particular, she mentions the Export Processing Zone Act of 1970, directing enterprises into manufacturing export-led growth, and subsidized rice and wheat flour, beginning in 1973-1974. Bräutigam finds the Mauritian model to be compatible with an equitable East Asian development model and observes that the export processing zones attract Hong Kong and East Asian investors. The strong orientation to export-led growth reflects awareness of trading activity as crucial to economic progress.

Yet, the freedom to trade internationally is limited in Mauritius (Gwartney & Lawson 2006). Mauritius chose a highly restrictive trade regime that segmented the export and import competing sectors (Rodrik 1999; Subramanian & Roy 2001). This kind of heterodox opening would not have been successful, unless Mauritius's trading partners had given Mauritius preferential access, thus benefiting from the protectionist policies of the United States and the European Union (EU), as Subramanian and Roy (2001) argue. In addition, they point out

that the Mauritian export processing zones benefited from the exemption from the prohibition of export subsidies under the WTO.

Mauritius belongs to both the Common Market of Eastern and Southern Africa (COMESA) and the Southern African Development Community (SADC) and has an economic partnership agreement (EPA) with the EU, like other SIDS COMESA members Comoros and Seychelles (Bilal, 2004). Similarly, several Caribbean SIDS constitute the Caribbean Community (CARICOM) and Asian small nations Singapore and Brunei Darussalam are members of the Association of Southeast Asian Nations (ASEAN) and the Asia-Pacific Economic Cooperation Forum (APEC), Singapore also having a bilateral trade agreement with the United States (Bilal, 2004).

Singapore was one of the founding members of ASEAN that in 1992 established the ASEAN Free Trade Area (AFTA), aiming at an ASEAN Community by 2020, made up by an ASEAN Economic Community (AEC), an ASEAN Security Community (ASC), and an ASEAN Socio-Cultural Community (ASCC). While participating as founding member of ASEAN in APEC to pursue trade liberalization voluntarily and the ASEAN+3 framework (ASEAN, China, Japan, and South Korea), Singapore is the regional champion of bilateral trade agreements, as a means to enhance global competitiveness through specialization and foreign direct investment (Cuyvers et al 2005). As Nesadurai (2002) argues, Singapore is the most active proponent of free trade areas in the region and its new preference for bilateralism reveals Singapore's impatience with the slow pace of trade liberalization in the AFTA. Nesadurai points out that Singapore's bilateralism goes beyond the WTO framework, thus constituting potentially a building block for global free trade. This illustrates Singapore's

very strong commitment to free trade, in contrast to Mauritius's heterodox opening. Free trade in a free market economy is in the long run crucial to the viability of small nations. However, as both Mauritius and Singapore illustrate, social cohesion and identification with economic development are also crucial.

A virtuous free-market economy calls for appropriate moral and cultural institutions, which evolve in the small group order of civil society, in accordance with economic personalism. Chang and Kozul-Wright's (1994) notion of national system of entrepreneurship consists of a set of institutions, which, on the one hand, encourages innovation and risk taking, but on the other hand, manages the destructive component of entrepreneurship. They find that South Korea pursued export competitiveness and upgrading of economic activity with the establishment of institutional links, including industrial and labor relations favorable to learning, like Sweden had done previously. However, they stress that the South Korean developmental state has been much more involved at the enterprise level targeting export performance of favored enterprises.

At independence in 1968, Mauritius was characterized by communal riots and heavy dependence on sugar cane exports, out of which emerged the idea of social harmony in diversity, the belief that both economic growth and social equity should be promoted, and labor-intensive, export-oriented industrialization (Bräutigam 1997). This represents a developmental state based upon coalitions. As Armstrong and Read (2002) argue, small nations possess greater social homogeneity and cohesion, flexibility, and openness and responsiveness to change. In Mauritius, the elites supported the development of export-led growth with equity (Bräutigam 1997).

At independence in 1965, Singapore was an underdeveloped country with widespread poverty, high unemployment, low levels of education, inadequate housing, communal violence, and industrial unrest, inducing consensus that sustained the developmental state, which created a stakeholder society (Sung 2006).

Mauritius had, at independence in 1968, an indigenous capitalist class of sugar planters and a middle class, but the Franco-Mauritian property holders were separate from the Indian and Creole middle class, out of whom Mauritian bureaucrats were recruited (Meisenhelder 1997). In addition, Mauritius's very strong civil society maintained interethnic harmony and therefore a very high level of participation among Mauritians as well as a general political willingness to compromise (Miles 1999). The idea of social harmony in diversity has been broadly shared and governments have been expected to promote social equity as well as growth (Bräutigam 1997). The sugar planters have provided a large amount of capital for diversification, while the developmental state focused on social security and welfare (Bunwaree 2005). Hence, Mauritius developed a national system of entrepreneurship promoting export-led growth and social welfare, thus making Mauritians identify with economic development. The separation of economic and political power has prevented the cash cow—the sugar sector—from being killed, while Mauritius ranks well above the African average with respect to all indices of institutional quality, thus explaining the success of the Mauritian export processing zones (Subramanian & Roy 2001). Mauritius is the only country in Africa that has been able to develop a pattern of rapid growth of manufactured exports (Söderbom & Teal 2003).

The idea of export processing zones, which institutionalizes export-led industrialization, reflects an East Asian inspired development strategy, where the Mauritian state guides and directs the markets (Meisenhelder 1997). Unlike Singapore that used forced saving rather than welfare programs and public housing to create stakeholding (Sung 2006), Mauritius has had a strong focus on social welfare, a heritage of Fabian socialism.

Education policy has been very different in the two countries. The education system in Singapore has been strongly focused on skill formation and long-term needs of the economy, involving more knowledge-based, conceptual, and adaptive skills to address the emerging knowledge economy and globalization (Sung 2006). However, the Mauritian education system wastes a large amount of its human capital, and those who succeed lack the skills required in the new knowledge economy, according to Bunwaree (2005). Productivity growth has become more important and upgrading of human capital through better skills and trade liberalization are crucial components (IMF 2001).

In spite of Singapore's position as the second most free economy in the world, according to Gwartney and Lawson's (2006) Economic Freedom of the World (EFW) rating, to which its very open economy contributes, its lack of natural resources, and its obligation to function within the global market system, Singapore is a very state-led society. In order to explain the economic success of Singapore, Sung (2006) develops the notion of developmental worker, who through continual personal participation, in exchange for current and more importantly future benefits; helps deliver economic growth that will realize the economic vision of the developmental state. Sung points out that the developmental state creates a stakeholder society, which yields the required

social cohesion to achieve economic growth targets, since the state-worker partnership requires a durable two-way relationship. This constitutes a viable system of entrepreneurship balancing creative and destructive elements of innovation.

According to Sung (2006), lacking natural resources, Singapore stressed skill formation from the very start. He identifies four phases aimed at: 1. creating a workforce for a manufacturing base in 1965-1979; 2. creating a skill upgrading strategy in 1979-1991; 3. targeting a higher position along the value-added chain in 1991-1999; and 4. tackling globalization and the knowledge-based economy as of 1999. This reveals a very adaptive approach aiming at survival, while climbing the value-added chain under global free trade.

Sung gives a detailed account of these four phases. The Singaporean government started by attracting inward investment from multinational corporations to establish manufacturing, which required education to create an adequate workforce, both in terms of skills and values, before turning into the second industrialization targeting investment with greater value-added. This involved a rapid skill adjustment process, stressing social cohesion and social discipline, but also investment in high-tech companies abroad to bring know-how back to Singapore. In order to climb the value-added chain, the developmental state turned to state benchmarking aiming at the Swiss living standard in 2020-2030, including a new skills upgrading effort, identifying the basic skills required for effective participation in an advanced industrial society and upgrading of vocational education. Finally, in order to adapt to the knowledge-based economy and globalization, Sung describes how the government aims at building knowledge-based, conceptual and adaptive skills through an integrated workforce development system

with the aim of building a workforce that can handle flexible work arrangements. Hence, Sung's (2006) image of the Singaporean model is a state-led continuous skills upgrading process through a state-worker partnership to climb the value-added chain.

Industrial clusters are also formed by the state. Yeung (2006) regards them as a deliberate and state-driven attempt to attract the location of high-tech activities of multinational corporations and local enterprises, using the Singapore Science Park as a means to develop research and development capacities, establishing a technology corridor around the National University of Singapore. Local small and medium-size companies have become capable of reverse technology transfer in their relationship with foreign multinational corporations, Yeung points out. Consequently, the developmental state in Singapore promotes by means of partnerships between foreign multinational corporations and local enterprises as well as between the state and the workers a continuous skills upgrading process guided by economic growth targets.

Self-realization through participation by entering into genuine community, along the lines of economic personalism (Santelli *et al* 2002), is an important characteristic of the developmental worker, but the morality of markets that emerges out of civil society is in Singapore a more deliberate state-driven process, unlike the very strong civil society in Mauritius. In Singapore, national values have evolved from social harmony as foundation of survival in the 1960s and early 1970s to Asian values with an emphasis upon indigenous cultures, religious education, Confucian ethics, and the cultural foundations of economically competitive society between the late 1970s and the mid 1980s, to communitarianism and shared values as of the late 1980s (Sung 2006). The latter were

formulated in a White Paper (1991) as shared values: nation before community and society above self, family as the basic unit of society, regard and community support for the individual, consensus and contention, and racial and religious harmony. Hence, the developmental state attempted at emulating civil society, in contrast to Mauritius's very strong civil society. As Boulding (1978) claims, behavior is a function of the image - the knowledge and value structure embodied in the human brain. The Singaporean developmental state has a strong integrative component and relies to a large extent on integrative power, including role, symbolic, and community power. This blurs the distinction between ideology and collective beliefs, as Sung (2006) finds to be a characteristic of a developmental state.

Singapore's strong commitment to free trade induces skills upgrading in order to remain competitive and climb the value-added chain, unlike Mauritius's heterodox opening with segmented trade liberalization, which the SIDS try to establish within the WTO framework, following the AOSIS Strategy. According to IMF (2001), Mauritius has made progress in liberalizing its trade regime, although significant import liberalization is required to achieve neutrality of incentives.

As Mauritius and Singapore illustrate, small nations have the capacity to be viable when a developmental state creates stakeholding in economic growth that together with civil society contribute to participation, based upon shared values. In addition to moral capital facilitating social cooperation, the education system must contribute to skill formation and continuous skill upgrading to achieve global competitiveness, which under free trade may become durable, unlike preferential treatment that gives less reliable market signals what skills are required.



## **Good Governance Matters: Why the Comoros Differs from Mauritius and Singapore**

Good governance is crucial to a developmental state in a free economy. The Comoros is, according to Walker (2007), one of the worst cases of state failure in Africa, in spite its cultural homogeneity. This can be contrasted to the African success story Mauritius, which is culturally heterogeneous, like Singapore. However, there are both a Mauritian nation and a Singaporean nation, while the same is less obvious for the Comoros.

Nation used to mean a linguistic community that could transform itself to a nation-state to facilitate public choices for the community (Jasay 1998). In the Comoros, no standardized national language has been consolidated, although Comorians understand each other, a socio-cultural unity without national identity (Walker 2007). Hence, in spite of an underlying cultural unity, there is not yet a nation that can be transformed into a nation-state. Although the Union of the Comoros officially consists of four islands, one of them, Mayotte, actually remained a French colony when the Comoros became independent in 1975 (Walker 2007). In the Comoros, one of the islands tried to break away from the other two in 1997 creating a secessionist crisis, which was settled in 2001 with a new constitution that established the Union of the Comoros (World Bank 2006). This started a stabilization process, interrupted by inter-island power struggle, but political instability has eroded the legitimacy and accountability of the state, which is absent at the local level (World Bank 2006). However, customary authority and structures remained strong (Walker 2007).

The Comorian nation-state lacks integrative power; the role, symbolic, community, and moral powers are all weak.

The autonomy of the country's constituent parts overrides the nation, state assets were appropriated by the elite, state symbols were commoditized, and the Comoros have enjoyed five national flags since 1975, (Walker 2007).

The performance on government effectiveness and corruption is particularly poor for sub-Saharan African standards (World Bank 2006). Recognizing the Comoros as a fragile state, the World Bank has developed an Interim Strategy for the Comoros to support constructive institutional change. According to the World Bank (2006), the main immediate obstacle to economic growth is the political situation, where inter-island tensions erode institutional capacity with corruption contributing to poor quality of government services and distrust in government, while remittances from the Comorian diaspora largely defines Comorian economy and society.

The new constitution of 2001 grants considerable autonomy to the islands, each of them has its own president and parliament, while a union parliament was not established until 2004 (World Bank 2006). This structure of three island presidents and parliaments with a union president and parliament gives the islands flexibility and autonomy (Walker 2007). Following Hume (1777), this would be favorable to learning with a free government. The Comoros has what Wagner (2007) calls multiple public squares. Wagner regards state and market as two arenas of interaction, the public square and the market square, respectively, and he argues that federalism potentially injects competition into the enterprises in the public square, along the lines of the market square. According to him, multiple public squares may accommodate different preferences among people and generate knowledge through experimentation. However, this requires some viability of enterprises in the public squares, which the

Comoros lacks. In addition, the lack of national identity means that competition between multiple public squares becomes less apparent.

The World Bank (2006) observes that projects implemented through the communities have been more successful than those implemented through the government. Customary structures, funded by remittances from expatriate Comorians in France, drives local development, not the state, and reciprocity established in customary exchange cycles provide welfare services (Walker 2007). The World Bank (2006) focuses on community and local capacity building for the provision of basic services, and on building state capacity and increasing accountability for consolidation of national reconciliation, but points out that civil society lacks skills and supporting infrastructure.

The Comorian state lacks all capacity to create stakeholding in economic growth, while national identity is very weak, thus limiting participation to local communities. Social cohesion, based on shared values, to promote global competitiveness of the nation is not even an issue, in contrast to Mauritius and Singapore. Moreover, the weak integrative structures due to a lack of national identity provide a weak support of exchange at the national level in the Comoros.

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Global Policy.

[www.globalpolicy.org/nations/micro](http://www.globalpolicy.org/nations/micro)

International Monetary Fund. [www.imf.org](http://www.imf.org)

Small Island Developing States Network.  
[www.sidsnet.org](http://www.sidsnet.org)

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## Social Democratic and Socialist Policies

*J.E. King*

Socialism is best defined very broadly, as the doctrine that capitalism has very serious problems, and that a substantial degree of public ownership is needed to solve them. On this definition, ‘socialism’ would include Marxists, Fabians, Utopians, Anarcho-Communists and even conservative (Bismarckian) State Socialists. Social democracy is an even more slippery term. In the late nineteenth century it was used by socialists of many persuasions, often but not always Marxist or Marxist-influenced, to express the conviction that society and the economy, as well as the polity, must be democratised. This was not seen as inconsistent either with the achievement of socialism through revolution, or even with a period of dictatorship after the revolution: in Russia, for example, the full name of the Bolshevik party was the RSDLP(B), or Russian Social Democratic Labour Party (Bolshevik).

After 1917, however, ‘social democracy’ was increasingly used to distinguish non-revolutionary or ‘reformist’ socialists from their bitter rivals in the international Communist movement. From 1945, it also came to connote a major revision of traditional socialist orthodoxy, involving a new commitment to a ‘mixed’ economy in which a large private sector would remain as a permanent feature. In the early 1980s the term ‘social democratic’ was appropriated by a right-wing breakaway from the (already very conservative) Labour Party in Britain, but by the end of the century it had fallen into disuse. It is best thought of today as characterising the economic policies that had been endorsed by non-Communist socialists in and out of ‘Labour’, ‘Socialist’ and (in some countries) ‘Social Democratic’ parties,

especially in Western Europe and Australasia, down to about 1980. On this definition, few if any centre-left parties are now socialist or social democratic, and, arguably, the Democratic Party in the US never has been. However, socialist and social democratic ideas are not dead. They continue to inspire Green parties around the world, though neoliberal thinking is increasingly in the ascendant there, too. They certainly resonate strongly in the global justice movement that erupted in the late 1990s, albeit radically altered to incorporate the so-called ‘new social movements’ (especially feminism), questions of environmental sustainability, and the global nature of the capitalist market.

In the remainder of this entry, the term ‘socialist’ will be used in a very broad sense to denote both social democratic and socialist ideas. For a general historical discussion, see King (2003b), Lichtheim (1983) and Sassoon (1996).

### **In The Beginning**

The most famous statement of socialist principles was written in 1847 by Friedrich Engels and Karl Marx. The *Communist Manifesto* emphasises the revolutionary and universal character of the capitalist system, which is inherently cosmopolitan and cannot avoid dissolving the national basis of production and exchange: ‘It compels all nations, on pain of extinction, to adopt the bourgeois mode of production’ (Marx and Engels 1998:244). It sets out a transitional programme for the working-class movement. The details would differ in different countries, Marx and Engels suggested, but the broad outlines were ‘pretty generally applicable’ throughout the world. Their demands included the abolition of private property in land; a heavy progressive income tax; abolition of the right of inheritance; centralisation of credit, and of the means of communication and transport, in the hands of



the state; an extension of factories and instruments of production owned by the state; a universal obligation to work; and free education for all children in public schools (pp. 257-8). In the *Communist Manifesto* it is taken for granted that the interests of working people are everywhere the same, and the concluding lines are intended as much more than mere rhetoric: 'The proletarians have nothing to lose but their chains. They have a world to win. Workingmen of all countries, unite!' (p. 268).

Half a century later, the Erfurt Programme of the Social Democratic Party in imperial Germany repeated these claims (Russell 1965:137-41). The global dimension was explicitly recognised. The proletariat faced the same problems, and had the same interests, in all capitalist countries. 'The liberation of the working class, accordingly, is a work in which the workmen of all civilised countries are equally involved', and the party therefore declared itself to be 'one with the class-conscious workmen of all other countries' (p.139; original emphasis). The detailed programme that followed included a demand for 'national and international legislation' to establish a maximum eight-hour day, to prohibit night work and child labour, and to guarantee at least 36 hours of unbroken rest for all workers each week (p. 141). Bertrand Russell commented at the time on the 'perfectly orthodox Marxianism' of the Erfurt Programme, 'and its boundless democracy' (p. 141). He might also have noted its moderation, and its global reach.

In the late 1890s, the 'revisionist' opponents of orthodox German Marxism argued that a proletarian revolution was both undesirable and unlikely to occur. Socialists ought therefore to be satisfied with the progressive, but peaceful, piecemeal and gradual, achievement of economic and social reform. In Britain the Fabian socialists took a very similar position. In both cases, however,

the cumulative effect of reforms was expected to be a fundamentally different social order (Webb and Webb 1920). The combined effect of the Great Depression and the (apparent) success of Stalin's industrialization of the Soviet Union radicalised Western socialists in the 1930s, temporarily increasing the appeal of a centrally planned economy under full public ownership. After 1945, however, a new revisionist current emerged, arguing that the socialist project must be adapted to take account of major changes that had occurred in the nature of capitalism. Some revisionists, like Anthony Crosland, even claimed that postwar Britain could no longer be described as capitalist. In *The Future of Socialism* (1956) he argued that ownership of the means of production was irrelevant, since large companies were now controlled by managers, not by shareholders, and the distribution of income depended more on politics (including taxation and government spending policies) than on market forces. For Crosland socialism was all about equality, not nationalisation. It is striking just how few references there are, in Crosland's 529-page book, to either finance or the world economy. He worries a little about the balance of payments (Crosland 1956:380-1), and expresses the hope that banks will lend more to industry (p.437-8), but that is about all: there are no references in the index to colonies, development, finance, international (anything), trade, world poverty or the World Bank. For Crosland, socialism was essentially a local matter, without significant global implications.

### **The Neoliberal Age**

This made sense only on the assumptions, firstly that the capitalist tiger had been tamed, so that the system had moved very much closer to socialism, and secondly that these changes were irreversible. Both proved to be false. In fairness to Crosland and his ilk, it should be stressed that the neoliberal

revolution that swept the globe after 1975 took everyone by surprise (Howard & King 2008). The neoliberals asserted that all social problems had a market solution, with deregulation and privatisation as corollaries. Financial markets, in particular, were to resume their pre-1929 importance, not actually to provide finance to companies (which still relied very largely on retained profits) but rather to ensure the maximisation of 'shareholder value' and to provide a market for corporate control.

All this was set in the context of a renewed capitalist globalisation, which should be seen not as an unavoidable Act of God but rather as a *project* (Quiggin 2001), reflected in the so-called Washington Consensus propagated by the IMF, the World Bank, the GATT (and its successor, the WTO) and by the US Treasury. Poor countries, especially, should rely upon free trade, unrestricted mobility of capital, free markets, sound finance, low taxes and a small public sector to achieve rapid economic development; and the rich countries would benefit from 'the magic of the market', too. The upshot was the steady dismantling of the post-1945 settlement by means of privatisation, cuts in welfare spending, big reductions in taxes on corporations and rich individuals, the lifting of restrictions on financial markets, and far-reaching attacks on labour market regulation and the power of trade unions. All this means that socialist and social democratic policy now has an unavoidably *reactionary* flavour, since its principal aim is to reverse the damage done by the neoliberals.

But it is not purely nostalgic. Indeed, it has been given added impetus by the global financial crisis of 2008. To cite one recent example, the crisis has prompted a statement by twenty prominent heterodox economists that includes demands for macroeconomic stabilisation, social justice, environmental

sustainability and international coordination of national recovery programmes. All would be recognizable to, and endorsed by, socialists and social democrats of earlier generations (Ash *et al.* 2009).

### **Public Ownership**

At least seven socialist arguments for public ownership can be distinguished. First, it is a necessary first step in the total transformation of society. Second, much more modestly, it enables particular industries to be run more efficiently. Third, monopolies should be in public ownership to prevent exploitation of consumers. Fourth, public ownership is needed to produce a more equal distribution of wealth (and this, in turn, is a pre-condition for real political democracy; the alternative is rule by the rich). Fifth, it is essential for macroeconomic stabilization, as only then can investment expenditure be varied to offset cyclical fluctuations in economic activity. Sixth, in industries producing *demerit goods* like tobacco and gambling, public ownership is the only way to give managers an incentive to restrict consumer demand. Seventh, large numbers of public sector jobs are needed if full employment is to be maintained.

The first argument is rejected by revisionist social democrats, and many other socialists now accept continuing private ownership of small business and actively encourage the growth of self-managed worker cooperatives (Nove 1983). Anti-socialists have always maintained that the other six objectives can be attained in other ways, by a combination of competition, regulation and taxation. These objections have some merit, but they completely fail to meet the macroeconomic case for public ownership (arguments five and seven) and ignore the political issues raised by regulatory capture and tax avoidance (which are related to arguments three and six).

The most interesting questions are those arising from the fourth argument. If highly progressive income, wealth and inheritance taxes can be imposed, and do generate a drastic reduction in the degree of inequality of wealth without old-fashioned 'nationalization' of the means of production, distribution and exchange, what sort of economy—and society—would this create? An egalitarian capitalism, along the lines of the 'property-owning democracy' that progressive conservatives have always claimed to support? Or a decentralized collectivism, with the great bulk of shares held by pension funds (Blackburn 2002) or union-controlled mutual funds (Arestis 1986)? Would there still be financial markets in such a system? How would they be regulated in the social interest? And how would such a pattern of ownership, and the corresponding system of regulation, be made consistent with the (often conflicting) demands of narrow economic efficiency and the broader concerns of social justice and environmental sustainability? Socialists still have a lot of thinking to do on all these questions.

One further socialist argument for public ownership deserves a mention. If there are binding political constraints on the amount that can be raised through taxation of corporate profits, public share ownership may be the only way in which society can obtain an acceptable proportion of total output (Quiggin 2001). On this argument, the privatization of highly profitable telecom enterprises (for example) was a mistake, whatever the merits of the efficiency, monopoly and macroeconomic arguments for their retention in public hands.

A final issue is especially relevant to socialism in the Third World, and this is land reform. Where the majority—or a very large minority—of the working population are peasant farmers, the distribution of landed

wealth is a critically important question. Socialists in Asia and Latin America therefore insist on the need to break up large estates and provide land to landless farmers, with an urgency unparalleled in Europe since the late nineteenth century.

### **Macroeconomic Stability**

For socialists, full employment should be the over-riding goal of macroeconomic policy. This entails what Abba Lerner referred to in the 1940s as 'functional finance', that is, tax and expenditure policy geared to achieving the full employment level of output, whatever the implications for public finances. If deficits (even large deficits) are required, so be it (Nevile 2003). But government deficits should be seen as at least in part, as an endogenous response to a collection of private sector decisions which in aggregate imply a private sector surplus. This points to the need to encourage private sector spending (Reynolds 2004), in particular by keeping interest rates low. Democratic control over monetary policy must therefore be re-established, with central banks coming back under parliamentary supervision and full employment replacing inflation as their chief priority. Central banks should target employment growth, subject to an inflation constraint. This is particularly important in developing countries like South Africa, where unemployment, open and concealed, is chronically at levels experienced in the rich countries only during the Great Depression. Here job creation is, literally, a matter of life and death (Pollin *et al.* 2007).

This has two implications. In the long run, output must grow at the (Harrod) *natural rate*, which is the rate that gives a constant unemployment percentage. In the short run a higher rate of growth will be needed to reduce unemployment to the maximum acceptable, or *full employment*, level, which in the rich countries might be as low as 2%. This initial



period of very rapid output growth raises the very real prospect of a conflict with environmental objectives, which require restrictions on the rate of growth of consumption. Environmental concerns aside, there will be an *inflation constraint* on the achievement of full employment, and in all likelihood a *balance of payments constraint* too. To overcome the inflation constraint, many socialists accept the need for an incomes policy, with an explicit commitment to maintaining (or perhaps increasing) the wage and salary share of GDP. Price and wage controls would be required, with a presumption that both wage-push and profit-push inflation are potentially important problems.

Balance of payments constraints can be dealt with in the long run through reform of the international financial system (Davidson 2008), and in the short run by re-regulation of financial markets and (where necessary) temporary increases in tariffs. An internationally-coordinated demand expansion would overcome the balance of payments constraint on individual national economies. It would almost certainly make the inflation constraint more serious, however, since the inelastic supply of primary products renders commodity prices sensitive to any significant increase in world demand, as became apparent in 2007 and the early months of 2008. Ussher (2009) draws on the work of Nicholas Kaldor to advocate a return to the commodity price stabilization schemes that operated with some success in the 1950s and 1960s, relying on internationally-administered buffer stocks (see also King 2009). This would benefit producers as well as consumers by preventing catastrophic price collapses like those suffered by cocoa and coffee producers in the late 1990s, and oil producers in the final months of 2008.

Sensible macroeconomic policies must be supplemented by compatible microeconomic

action, including detailed intervention in financial markets to regulate the allocation of credit. One relevant proposal is for the introduction of differential reserve requirements, favouring employment-generating investment at the expense of speculation. Asset-based reserve requirements would also allow some control of asset price bubbles (Palley 2004).

### **Social Justice**

A return to full employment would be the single most important contribution to social justice that economic policy could make. This almost certainly involves substantial public employment programmes, with the government acting as employer of last resort, offering jobs to all who are willing to work and unable to find private sector employment. Socialists would expect those employed in this way to receive union-negotiated wage rates appropriate to their skills. More conservative proponents of the 'job guarantee' would offer only minimum wages (Wray 1998).

Improvements to social welfare also involve continued public provision of pensions and other income maintenance payments, and the supply of much greater quantities of public goods like health care, education and child care by not-for-profit institutions that are subject to democratic supervision and control. There must also be a firm commitment to gender/ethnicity equality and the reversal of environmental decay (which affects the poor more than the rich). Productive public investment in these and similar fields would stimulate private investment in related activities, leading to 'crowding in' rather than to the conservative bugbear of 'crowding out'.

Socialists also support re-regulation of the labour market to reduce inequality in employment incomes, restrict hours of work and encourage industrial democracy. They are

natural allies of trade unions and supporters of collective bargaining, but recognise that there are increasingly severe limits to what can be achieved through bargaining by weak unions, and a corresponding need for political intervention to enforce the payment of a living wage (Pollin *et al.* 2008) and employer acceptance of reasonable constraints on working hours. This could be widened to include a much broader demand for industrial democracy. Co-determination has proved sufficiently unpopular with German business to suggest that there might well be something in it for labour, especially if it is combined with an interventionist industry policy giving employees some control over corporate investment decisions. The 1980s Swedish proposal for wage-earner funds—a form of collective profit-sharing with substantial union involvement—also deserves reconsideration as a means of reducing inequalities in income and wealth without exposing working people to excessive levels of financial risk (Arestis 1986). An alternative is employee ownership of the individual enterprise, which would greatly reduce the need for supervision and monitoring of the workforce and therefore significantly increase labour productivity (Bowles and Gintis 1998). This, however, is open to the powerful objection that working people cannot afford to have all their limited financial eggs in one fragile basket.

Statutory limitations on excessive working hours have already been imposed in the European Union, and they have been effective, up to a point. They should be supplemented by measures to reverse the pressures of workplace culture that contribute to the acceptance of overwork by those who suffer most from it, including family-friendly policies that encourage parents to spend more time with their young children. The restoration of full employment will make this easier, as it will substantially increase the

bargaining power of labour (unionised or not) at the expense of capital.

One longstanding proposal with impeccable socialist credentials (Russell 1918; Meade 1989) is the payment of an unconditional Basic or Citizens' Income, financed by progressive taxation. Since it offers an alternative source of income to paid employment, Basic Income has a number of important advantages. It would value the work of carers (who are mostly women), and encourage leisure and voluntary work at the expense of consumption. It would, however, be extremely expensive, especially if set at a level significantly above the bare requirements for subsistence, in which case it would probably have a significant impact on work incentives (and corresponding environmental benefits in reducing the full employment or natural rate of growth of output). A more conservative version of Basic Income would pay it only to those actively engaged in socially desirable non-market activities, including the care of young children or elderly relatives.

### **Tax Reform**

Increased public expenditure will place pressure on government finances, so that tax reform is important. Uncontroversially, this must include better enforcement of the existing system (closing loopholes and attacking tax havens). It will also require the 'green taxes' detailed below and substantial taxation of wealth, especially (but not exclusively) inherited wealth. Taxes on land should be substantially increased, and a case can also be made for the replacement of taxes on income by a progressive expenditure tax along the lines suggested many years ago by Nicholas Kaldor (1955).

There is an urgent need to eliminate tax competition between nation-states, which generates a fiscal 'race to the bottom' and reduces the revenue-raising potential of them

all. Thus tax policy has an inescapable global dimension. This is acknowledged by the many socialists who campaign for the introduction of a financial transactions tax, either restricted to foreign exchange dealings, the so-called Tobin tax (Patomäki 2001), or a more general tax on all financial transactions. Patomäki argues that the technical difficulties of implementing the Tobin tax are often exaggerated. In particular, it does not require unanimous international endorsement, but could initially be introduced by a grouping of states, such as the European Union, with other national governments joining the proposed TTO (Tobin Tax Organisation) at a later date. Since the tax is unlikely to eliminate currency speculation altogether, this offers the prospect of very significant increases in government revenue (see Davidson 2002:ch 12, for some objections).

### **Environmental Sustainability**

Socialists are less sharply divided from conservatives and liberals on environmental questions than on any of the other issues. The fundamental neoclassical principle of scarcity does after all apply to nature, whereas it is relevant to labour only in wartime and no-one has ever been able to make analytical sense of the notion of 'scarcity of capital'. Most non-socialist economists will agree that the internalisation of environmental externalities has not gone very far; that the Coase theorem is almost entirely useless as a solution to global warming; and that some elaborate combination of regulation, taxation and subsidies will be necessary to bring marginal private costs much closer to marginal social costs, and marginal private benefits much closer to marginal social benefits, than they are at present (Pearce 1993).

There is thus a very strong case for a redefinition of total output, replacing (or at least supplementing) GDP with measures reflecting environmental goods, leisure, non-

market and voluntary work. Many socialists would go further, urging a reduction in the level of consumption in the rich countries of the world and a corresponding repudiation of the consumerist ethic that dominates them (Victor and Rosenbluth 2007). They would also endorse a fundamental reform of the taxation system to tax environmentally damaging activities: the carbon tax is the best-known proposal, with salination and water use taxes not far behind. But socialists place less emphasis on taxation, and more on direct regulation, given their well-founded objections to the neoclassical analysis of substitution in consumption and production. There are also sound reasons for rejecting market prices as indices of scarcity, again contributing to socialist scepticism concerning market-based solutions to environmental problems (Winnett 2003). Tinkering with the price mechanism is unlikely to be sufficient; a more fundamental change in human behaviour, values and styles of life may well be necessary to protect the environment in the longer term.

Socialists are, however, divided on the merits of a steady-state economy (zero growth) as a medium- or long-term goal. At least for poor countries, a substantial period of rapid growth seems essential in order to secure a decent life for the great majority of the population; redistribution from rich to poor is necessary, but not in any way sufficient. Assuming for the moment that eliminating growth is desirable, there are two potentially very serious problems. In the short- to medium-term, there is the previously-noted difficulty of reconciling zero growth with full employment. In the long run, if productivity growth is a function of output growth then accepting a steady-state economy might require us to renounce dynamic economies of scale, posing problems for international competitiveness and worsening the balance of payments constraint

on employment policy in any individual country. 'Environmental responsibility in one country' may therefore be impracticable for narrowly economic reasons alone, quite apart from the global nature of ecological systems.

### **International Responsibility**

Socialists see an urgent need to reform international economic institutions to make them democratically accountable and remove their pro-corporation, deflationary, neoliberal biases. In the case of the IMF, World Bank and WTO this may well require their closure and replacement by entirely new institutions capable of making an entirely fresh start. At the very least, the lending advice and conditionality imposed by the IMF must be changed, and global counter-cyclical policy promoted (Ash *et al.* 2009). Opposition to any extension of the WTO's General Agreement on Trade in Services is also essential if social welfare provisions are to be protected. Socialists also call for re-regulation of international financial markets, and many would welcome a return to fixed exchange rates and (perhaps) the restriction of all foreign exchange transactions to central banks (as proposed by Davidson 2002). Short of this, Patomäki proposes a two-tiered Tobin tax, with the higher rate automatically applying in periods of increased currency volatility to dampen the incentive for further speculation.

A number of more contentious suggestions will require further discussion. Among the most divisive is the question of alternatives to free trade that could protect the interests of low-income groups in both the rich and the poor countries. Socialists in the Third World agree with liberal internationalists in the West that the subsidies paid to farmers in the US and the European Union have had devastating consequences for peasant agriculture in poor countries, and should be eliminated in the interests of global justice. Western socialists

accept the underlying indictment, but might have worries about the implications for small farmers, and low-income rural communities, in the West.

Sharper divisions arise on the question of trade in manufactures and, increasingly, in services, where the interests of the working class in (for example) Western Europe and China are very difficult to reconcile. Thomas Palley distinguishes trade between countries with similar wage levels and socioeconomic systems ('developed-developed free trade') from trade between countries where both wage levels and socioeconomic systems are radically different ('developed-underdeveloped free trade'). The latter, he argues, does not necessarily benefit working people in the more developed country: 'In effect, free trade serves to unify the labor markets of developed and under-developed countries, and this puts strong downward pressure on wages in the developed country. ... In this fashion, free trade worsens income distribution' (Palley 1998:166). It also reduces workers' bargaining power, undermining the socioeconomic structure and encouraging a further 'race to the bottom' in employment standards. Palley suggests that a 'social tariff' might be imposed 'to compensate for low wages and lack of commitment to social goals regarding the environment, worker health and safety, and social welfare'. The revenue might then be redistributed back to the developing countries (Palley 1998:171).

Palley's proposals for the avoidance of 'social dumping' reflect what Graham Dunkley has termed the 'Fair Trade' alternative to free trade. Significantly, Palley does not endorse the more radical, 'unit cost equalisation', variant of Fair Trade, 'based on the specification of minimum wages and conditions, though not actual wage rates, the aim being to minimise international "unit cost gaps" as calculated on the basis of relative

productivity and real wage rates' (Dunkley 1997:252). The problem with this, of course, is the impact on employment opportunities in the poor countries. Huge issues arise here concerning the conflict of interest between workers in rich and poor countries: the latter would gain if free trade were in effect to create a single unified global labour market, while the latter would lose, and lose disastrously. A Rawlsian would therefore be inclined to favour free trade, but almost no-one in the rich countries is a Rawlsian at the global level. For very similar reasons, none but the very rich favour uncontrolled immigration, however strong the moral case for such a policy might be. Unfortunately Marx and Engels were wrong: the interests of workers in all countries are *not* the same.

Fair Trade is not the only alternative to free trade. Dunkley discusses several forms of 'Managed Trade', and also what he terms 'Self-Reliant Trade', which offers 'a chance to be one's self', and 'seeks only to eschew heavy trade dependence for key capital, consumer, food, energy, cultural or social requirements' (*ibid.*, p.255). Short of a comprehensive, binding international agreement on environmental sustainability, this may be the only way in which respect for nature can be reconciled with the brutal facts of learning-by-doing and dynamic economies of scale.

## Conclusion

Socialists agree that the market, while potentially a good servant, has become a very poor master. The triumph of neoliberalism, they argue, has been accompanied by growing inequality (within and between nations), mass unemployment, macroeconomic instability and unsustainable environmental destruction. In political terms, it has also undermined democracy and generated a sinister tendency towards global plutocracy. Socialist policy therefore involves

a substantial extension of public ownership; the restoration of full employment; a commitment to increased economic, social and political equality; fundamental tax reform; a strong focus on environmental sustainability; and, last but not least, acceptance of international responsibility for global justice. This represents a real intellectual alternative to neoliberalism, but it is too early to say whether it also poses a significant political threat to the status quo. Much will depend on the consequences for the real economy of the 2008 global financial crisis. A severe world recession would greatly increase the political appeal of socialist and social democratic policies like those proposed here.

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## Theories of the State

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### **Introduction**

The recent, unparalleled ascendancy of the liberal democratic state may seem to render alternative theories of the state redundant. But while the prevailing view might be that “I have seen the future, and it works”, it was not so long ago that this was said about a very different type of state.<sup>i</sup> And while the liberal democratic state is an abundant form of government, in practice this often reflects an uneasy compromise of conflicting conceptions of politics. It thus remains important to unpick the theoretical underpinnings of conceptions of the state.

A great attraction of the liberal democratic state is its promise to reconcile the myriad of competing claims about the direction of society. With parallels to the “invisible hand” of the market, the liberal democratic state weighs the expressed interests of particular business, labour, ethnic, religious and other affinity groups, judiciously determining a course of action to accommodate these, thus reflecting the general interest of all. A popularly elected legislature combined with civil liberties comprises the key mechanism to ensure that the collective interest is pursued.

Yet many contest the vision of the state as neutral social arbitrator. For classical liberalism, *any* state activity beyond a minimal defence of contracts among free agents infringes liberty. For conservatism, neutrality is moral abdication; the state has a duty to provide leadership in social values. For social democracy, neutrality is not possible if citizens have unequal access to the political system; the state must act positively to create the conditions for neutral arbitration. For Marxism, the economic and social power

of business precludes and thus excludes all other interests.

These alternative conceptions of the state continue to challenge liberal democratic theory and while many states have a liberal democratic form, their actual practice often derives from some variant of these alternatives. While the purest practical expression of the liberal democratic state can be found in the United States and Britain, classical liberal and conservative practices are also evident. In Continental Europe, the social democratic “Social Model” strongly informs the practice of liberal democratic states there. Conservative practice is a major feature of liberal democratic states in much of the Third World, where representative government and civil liberties often remain fictions for much of the population (see Moran 2001).

### **Liberal Democratic Theory of the State**

The concept of the state representing the “general” or “national” interest of citizens has classical liberal origins. Against the feudal belief in the divine rights of the royalty and aristocracy, classical theorists argued that state authority is founded on the will of individual members of civil society. Individuals explicitly or tacitly submit to the authority of a state as the means to affect their collective interests (Hobbes 1968; Locke 1977; Rousseau 1973; Hegel 1991). In classical theory, representation is not universal, however, but is limited to members of civil society, that is, citizens possessing property (Locke 1977; Rousseau 1973). Furthermore, the state can diverge from the general interest of civil society and so needs to be checked by democratic processes (Locke, 1977; Smith, 1976; Bentham, 1948; Mill, 1937; Mill, 1962; see also MacPherson, 1962; 1977). In essence, though, the state is assumed to be largely neutral and to act on it’s own view of the “national interest”; there is little examination of the policy-making



process within the state, the assumption being that policy is formed by the application of rational minds to problems (Clegg *et al.*, 1986).

Liberal democracy can be distinguished from classical liberalism by the wider ambit recognised for the state and the greater attention given to the representation of specific social interests and the mechanisms of policy-making. These pluralist approaches, foreshadowed by Hamilton *et al.* (1948), emerged from Weber (1978) and were given impetus by Michels' (1949) identification of elite domination of organisations. Disputes exist within this approach about the degree to which the elite is open or closed. Dahl (1956), for example, argues that all citizens have the capacity to accumulate sufficient resources to influence the collective policy decisions they wish, whether by voting or more vigorous campaigning, and thus no individual can monopolise this influence, provided civil liberty existed. Truman (1951) extends this approach to organised "interest groups", arguing that no single group can have a monopoly of influence because of the potential for existing or latent countervailing interests to assert their influence. The liberal democratic state is not simply a weather-vane amidst these influences, however, but judges competing claims with an eye to the principles of civil liberty.

A less sanguine view admits the pluralist mechanism but sees the elite closed to outside interests. Business, in particular, is seen to have a privileged access to the state through historically close personal connections and often a "revolving door" between employment in state and business management (Hunter 1953, Mills 1956, Domhoff 1967, Useem 1984). A feminist variant (MacKinnon 1989) defines the elite as male, noting that while states have at times repressed men, they have never done so as "men" in the way that they have done so to

women. Even with a closed elite, however, it can be argued that major countervailing interests can be effectively represented through corporatist arrangements, such as formal "tripartite" consultations between business groups, trade unions and the state (Schmitter & Lehmbruch 1979).

Opinion on the degree to which the elite is closed has ebbed and flowed with the tide of empirical investigation. Recent identification and analysis of policy networks of social interests, influencers and decision-makers around and within the state the state has provided a higher degree of specificity to such questions (Knoke 1990, Marsh & Rhodes 1992). In general, elite theoretic approaches share the pluralist conception that the state, or at least state officials, are independent agents, albeit within democratic, social, or economic constraints, that is, they are "relatively autonomous" (Block 1977).

Division remains over the extent of the constraints. Neo-pluralists and elite theorists argue that business decision-makers, in particular, have an effective veto over state policy via "business confidence" (Offe 1974). Business leaders have greater power than recognised in simple pluralist analyses because of their day-to-day control of the economic processes that underpin society, power no other group has. Nor does this power require much collective organisation to be effective, as capital flight and reluctance to invest quickly gathers its own momentum. Thus "a major function of government ... is to see to it that businessmen perform their tasks", often by inducement (Lindblom 1977:172-6).

Yet within this framework, it is not clear that business interests do have more weight in the policy making process than state officials. In developing countries, in particular, state officials are likely to have considerably more weight than business leaders because the business classes are weaker against both

international forces and local workers and peasants (Evans 1979). Further, state officials in the third world preside over strong states often with close military ties (Skocpol 1978). Even in developed countries, intense conflicts between business interests, together with the considerable resources available allows the state to routinely isolate itself from the lobbying approaches of particular interests (Crouch 1979; Nordlinger 1981; Evans *et al.* 1985). However, what is defined as the independent position of the state in this work, is often indistinguishable from the outlook of the financial sector, perhaps testimony to influence at a deeper institutional level (Duménil & Lévy 2004). The concept of relative autonomy of the state and the neo-realist claim of complete autonomy do not seem too far apart.

### **Globalisation**

At the same time as increased attention has been given to the ability of the state to insulate itself from the demands of particular interests in society, the very capacity of the state to resist external influences has been questioned. The globalisation thesis poses international markets, transnational corporations, and international institutions such as the IMF and WTO as powerful homogenising forces on nation states, with governments little able to resist this (Ohmae 1990). Reduced regulation and taxation of business and reduced state provision of services are a virtually inevitable result.

While this argument has been associated with neo-liberalism, a variation has been embraced by postmodernism as well. Here, globalisation has not only radically undermined the nation state but also hierarchies in general. Power is not restricted to the state nor even particularly important there but is pervasive and in a complex intertwined manner throughout social relationships at all levels (Foucault 1979).

“Fordist” vertically integrated mass production is being eclipsed by flexible production, the transnational hierarchy by the “network enterprise”, the state by localised power relations, national and class identities by personal affinities (Piore & Sabel 1984, Castells 1996, Hardt & Negri 2000).

Suggestions of the demise of the nation state, however, appear to be overstated. Government policies retain considerable national distinctiveness and state services remain a substantial component in most Western economies. The increased capital mobility in the 1980s and 90s was largely restricted to financial markets while global economic transactions remain concentrated among the triad of the US, Europe and Japan. In fact, the international liberalisation of the 1980s and 1990s has many parallels with a similar period of liberalisation a century earlier, a period followed by renewed regulation and prominence of the nation state. Further, the powers of international institutions remain dependent on member authorities and represent policy coordination mechanisms rather than abrogations of sovereignty. And empirical investigation suggests the flexibility and responsiveness of current productive systems is overstated (Hirst & Thompson 1996; Hay & Marsh 2000; Williams *et al.* 1987).

### **Neoliberal State Theory**

Drawing on Austrian economic interest in the role of markets in information transfer and notions of transaction cost economics, collective or public choice theory has turned attention from the influence of external interests on state action to that of internal interests. Public choice theory seeks to explain the origins of state policy in the actions of bureaucratic or professional interest groups within the state and proposes a range of governance mechanisms to limit

their influence (Olson 1965,1981; Krueger 1974, Bates 1981).

From the public choice perspective, administrative coordination is a costly activity. It can be very difficult to replicate the ruthless discipline of the market by administrative means, particularly in terms of dynamic efficiency, or continuous improvements in productivity. Vertical integration limits the ability to gain the benefits of specialisation available to independent producers and costs are incurred by mistaken integration, that is, producing goods or services in-house when cheaper sources are available externally (Masten *et al.* 1991).

A particular source of costs associated with organisational coordination are those posed by the principal-agent problem (Ross 1973). This is the recognition that there are costs involved in ensuring that agents outside immediate direction act in the intended manner. The archetypal example is the relationship of the chief executive officer of a firm to the owners of the firm; while the owners may seek the maximum return on investments, the chief executive may prefer to pursue personal goals of salary, benefits or status instead. The problem is greatest when agent performance is ambiguous as the costs of monitoring agent performance are high, that is, there is hidden information or a “moral hazard” present (Homström 1979). In these conditions there are greater opportunities to “shirk”, that is, avoid the set tasks, or “free ride” on the efforts of others (Ross 1973, Olson 1965). An indication of costs associated with the principal-agent problem is given by Krueger’s (1991) finding of a fall in profitability following vertical integration of fast-food stores from 9.5 percent to 1.8 percent. Public choice theory suggests the principal-agent problem is endemic in the relationship between government and state employees. But this

claim is fiercely contested on grounds that the strong public service ethic among state employees profoundly dilutes the rational egoist calculus underpinning the argument (Sheaff & West 1997; Chapman 1988).

The themes of neo-liberal public choice theory resonate with those of classical liberalism and are often intertwined with theoretical justification for a reduction in the scope of state activity towards the “night watchman state” (Nozick 1974). But it is also compatible with a strong authoritarian state, Hayek (1978) arguing that the causes of economic decline cannot be reversed with a minimalist state.

### **Institutionalism**

The contrasting views of the autonomous power of the state and its external and internal limitations have been somewhat reconciled recently by the notion of increasing the capacity of the state to act purposively (Frieden 1994). Rational-choice based “neo-institutionalism” emphasises the way “supply side” institutionalised rules and procedures order the preferences of policy-makers (March & Olsen, 1989; Shepsle, 1989). This is congruent with various analyses of the “demand side”, the, often unequal, social origins of institutions and procedures (North & Thomas 1973; North 1984; Olson 1981; Kingdon 1984; Baumgartner & Jones, 1993; Mucciaroni 1995). Institutionalism extends, and arguably transcends, the abstract rational egoist that underpins neoliberalism, with the concept of the socially embedded individual, institutional context constraining and empowering individual choices.

Yet such approaches tend to reduce state activity to an institutional determinism. On the one hand, this provides little consideration of the way that individual actors negotiate institutional arrangements. On the other hand, it overstates the impact of state institutions and individual actors in comparison to

broader social influences. Many Western states, for example, have had little difficulty in enhancing their capacity to police Islamic dissidents in the context of broad social support for this. By contrast, attempts to reduce state provision of health care and superannuation in Europe have been much more problematic for the same states because of wide social opposition.

### **Marxist State Theory**

Where orthodox state theory admits varying degrees of influence from specific interests, Marxist state theory identifies a pervasive influence of social classes on the state. The representation of specific interests is not restricted to the leaders of government, the state bureaucracy, closed elites, or an open range of interests, as in orthodox state theory. Rather, systematic biases towards particular class interests are seen to pervade the state. Like neo-realist, neo-liberal and institutional versions of pluralism, Marxist state theory generally recognises the significance of the institutional framework of the state, but attempts to ground these institutional forms in social conflict.

Yet, echoing orthodox state theory and no doubt because of considerable ambiguity in the original formulations, the Marxist approach has been haunted by disputes about the degree of autonomy of the state with respect to social influences. In common with pluralist elite theorists, many Marxist state theorists have sought to identify mechanisms by which business interests are imposed on the state, thus emphasising the concept of the state as an “instrument” of the ruling class (Aaronovitch 1956, Miliband 1969). Evidence of the state often acting against the expressed wishes of particular capitalists or interest groups, however, has fuelled opposing structuralist theories. These seek to explain state activity by the conditions necessary for capitalist social relations as a

whole to be reproduced from one day to the next (Althusser 1971, O'Connor 1973; Gough 1979). But in the absence of explanations of how state officials come to know the structural imperatives of capitalism, the latter approach tends to reduce to functionalism.

The central focus of neo-Marxist state theory has been to attempt to explain the specific institutional forms of the state in terms of social conflict, without falling into either instrumental or structural-functionalist explanation. However, derivation of the state form from the “needs” of capital accumulation (Holloway & Picciotto 1978, Reuten & Williams 1989) do tend to collapse into functionalist explanations and overlook state activity that may cause difficulties for capital such as elections and bureaucratic obstacles (Jessop 1977, Clarke 1991). Even sophisticated attempts to explain particular forms of state in terms of comprehensive regimes of accumulation and modes of regulation such as “Fordism” and “Post Fordism” (Aglietta 1979, Lipietz 1982, de Vroey 1984, Hirsch 1985, Jessop 1988) display a tendency to reify the particular “regime” over the social relations underpinning these. The approach also seems particularly susceptible to Laclau’s (1977) charge of “taxonomic fury” (Harvey, 1989; Bonefeld, 1993, Clarke, 1992).

The neo-Marxist approach is more readily apparent when the state is conceived as a form of social conflict. The argument here is that the state does not have power independent of its social context and thus is no more autonomous from the capitalist class than the firm is. Both are forms of capitalist power and the particular institutional arrangements are contested by different groups of capitalists and other classes. The “power of the social classes is organized in specific institutions which are power centres ... the state is *the centre of the exercise of political power*” (Poulantzas 1973:115).

An initial implication of this approach is that, while the state is a focus for the exercise of power, the state is institutionally incoherent because of unevenness of social conflict (Poulantzas, 1978). But the variety of individuated encounters with capitalist power are fetishised as the actions of a rational unified autonomous entity, the state, in a similar manner to the way that Marx argues the idea of God appears to the dispossessed (Mitchell 1991). This is not to say these forms are illusory; they have concrete effects but derive their content from social relations. “The wage contract between individual worker and capitalist is a very solid reality if the capitalist has the power to enforce that contract, but dissolves into pure illusion if the workers are able to counterpose their collective power to that of capital” (Clarke 1991:45).

A second implication of the neo-Marxist approach is while the concrete institutions of state, are constituted outside and above any particular interest in society, there is no autonomy from social conflict as a whole (Poulantzas 1973). At the same time, the separation from particular interests makes influence or control of state institutions attractive to those interests. Hence the reality of pluralist struggles over state institutions, problems of agency and concern for the capacity of these institutions to maintain relative autonomy from these. Yet the prize is as fleeting as individual advantage in the share market, which is always derived from the market as a whole.

Thus state capacity cannot be “increased” in an institutional sense, abstractly; the capacity of particular state institutions to act is always a function of the particularities of social conflict. In other words, concern to increase state capacity in general is a desire to strengthen the position of the capitalist class in conflict (Barrow 1993). In fact, if power in society is seen as the determinant of state

activity then “strong states”, with their limited tactics, actually indicate a perilous vulnerability among the dominant social groups, and hence the temporality of this resort.

Thirdly, liberal democracy is the normal form of capitalist state because it works for business. The separation of state and economic activity allows capitalists to concentrate on increasing the productivity and profitability of industry and commerce by delegating regulatory matters to specialists (Marx 1992). The principle of equality before the law derives from and supports free exchange necessary for market transactions. Separation of legislature, executive and judiciary guarantees both to some degree (Holloway & Picciotto 1978). And liberal democracy constitutes socially interdependent producers as individuated, albeit represented, citizens, separated from each other and the means of production (Poulantzas 1976).

However, fourthly, while liberal democracy may be the normal form of the capitalist state there are different varieties of liberalism. The Keynesian Welfare State accommodated and co-opted well-organised labour and legitimised capitalist growth through the early post-war era. Later, however, the challenge of accommodating working class aspirations through increased social welfare provision in periods of accumulation difficulty are highly conducive to authoritarian state practices, and a shift in the locus of state activity from the legislature to executive, as seen in the Thatcher and Reagan periods (O’Connor 1973, Habermas 1975, Poulantzas 1976).

Conditions of subsequent working class defeat do not demand a return to welfare provision and corporatism, however, as this is a co-optive strategy necessary only when faced with a strong opponent. Rather, as argued by various contributors in a recent compilation by Aronowitz and Bratsis (2003),

an authoritarian liberalism is much more conducive. Here the locus of state activity shifts from the executive to judiciary, repressing working and living conditions at the micro- and family-levels, but on a clearly defined non-discriminatory basis, as with workfare and “deserving poor” policies. Yet at the same time corruption among capitalists is endemic (Bratsis 2003). Thus, the widespread defeat of organised labour and the associated decline of labour-aligned political parties allows the widespread domestic pursuit of a repressive political strategy that appears as the international spread of a Anglo-American model through “globalisation”.

### Assessment

The conception of the state as a form of wider social conflict and attention to the specific form of the state provide a useful means to overcome the dichotomy between individual agency and functional-structuralism that tends to dominate state theory. But, to avoid the tendency for state form explanations to collapse into one or other of these extremes, the trajectory of these social conflicts outside and within the state form need to be given central attention.

This is not a matter of identifying simple interests such as the association between financial interests and neoliberalism (Duménil & Lévy 2004, Thompson 1977) but rather “constellations” of interests, for example found by Schmidt (1982) determining many economic policies, or in foreign policy (Mitchell 1991). Here again Poulantzas’ notion of “power bloc”, employing the Gramscian notion of hegemony, is useful. The contemporary conception of “policy network” appears amenable to reframing in such terms.

Such an approach anchors the state as an *internal* component of social conflict, rather than an *external* subject above society. Then

the state is not conceived as a passive instrument of interest groups, elites or the ruling class or the necessary reflection of a social function or structure. Instead, as an active site of power struggles in society, the specific institutions and actions of the state are constituted by social conflicts.

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## Undemocratic and Authoritarian Governments

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### **Introduction**

Over the long sweep of history democracies have been decidedly uncommon. At the moment, somewhat more than half the human race lives in the democracies, but that number is heavily dominated by the poverty stricken citizens of India. Further, from the establishment of independence in India until very recently the government of India was economically inept. The Indian economy was unable to provide either a high living standard or a rapid growth until the Congress party was replaced by the present coalition. Under the present government they are doing better, but that is weak praise.

The other very populous nation, China, is currently growing very rapidly. But the current rapid growth is only very recent. When the Communist government was established they began by a mass murder of landlords and then collectivized the land. Then followed the "great leap forward" in which Mao Tse Tung's ideas on agriculture were demonstrated to be probmenatic. The death toll is estimated at about 50 million, the worst famine ever experienced by the human race. India at any event escaped this kind of catastrophe. When Mao died and was replaced by Deng Hsiao Ping, China went from an effort to impose communism to an effort to move toward capitalism. So far this has been spectacularly successful, but China was so poor when it was inaugurated that it is currently probably no better off than India. It does however have a very rapid rate of growth whereas India's rate of growth, if at least better than that under the Congress party, is still mediocre.

It's hard to say whether this record shows democracy for populous and poor countries as

good or bad. Further under the Congress party India came close to being a constitutional monarchy. The same family provided most of the prime ministers until the last male member of the family was assassinated. The crown then passed to the only remaining member of the dominant family, who was not only a woman, but an Italian. She lost an election and the present coalition took power. Thus the democratic history of India is not all that encouraging. On the other hand, if we leave India out, the remaining world population is heavily undemocratic in its government.

There is also a sort of intermediate stage. We've already discussed the situation in the United States before the 1960s in which not all adults could vote. In the United States this appears to made little difference in the actual functioning of the government. Blacks, of course, were first enslaved and then subject to severe discrimination and women did not have the full legal rights of men. If we look at the structure of government however it was not much changed when these two types of discrimination were eliminated. Blacks, and to a lesser extent women, still feel strongly about this, and there is no reason they should not. Nevertheless the actual structure of government remains much the same.

We shall deal with these other forms of government in this chapter. Firstly we will deal with absolutist governments that may be divided, roughly speaking, into two categories. There are dictatorships and monarchies. This distinction is one that is rarely mentioned, but I think important. Basically it is the method of replacement of a former ruler. In monarchies there is a regular system, usually hereditary. In dictatorships it's a question of who wins the fight to rule. Frequently a dictatorship will eventually lead to the establishment of a monarchy with the descendants of the original dictator as the King, Emperor, or prince.

Although dictators are common enough historically, monarchies are much more numerous. Why this is so we will see after we have completed the discussion of dictators. The intermediate stage in which the government is elected but in which the electorate is severely restricted will be dealt with at the end of this chapter. Most political science books ignore it, but it is interesting, and in several cases has been very effective.

### **Dictatorship**

Turning then to dictatorships, the dictator must, of necessity, be a very capable man. He has obtained his dictatorship by climbing the slippery pole. He has outmaneuvered other contestants for the throne, escaped no doubt many efforts to kill him, and must continuously suspect all of his higher officials of trying to replace him. Normally he is apt to be, intelligent, devious, and hard working. Whether he gives his subjects a good government is an open question. Augustus Caesar certainly did. Further according to Gibbon the four adoptive Emperors produced the best government the world had seen before his time.

Mexico tried something like this for number of years beginning in 1931 and ending with the election of the current president. The president served his constitutional term of six years, and then appointed a successor. On the whole this seems to have worked out reasonably well. Of course, the President did not have the full powers of a dictator, and this may have made the difference. Further although the government of the Party of Revolutionary Institutions gave Mexico a not bad government by the standards of Latin America, no one would say that it was really a good government.

Turning to the more ordinary dictatorships, today they are the most frequent form of government. In some cases, like the Congo

it's hard to argue there is any government at all. Still in most cases, like Pakistan, China, and almost any of the Turkish governments, which have succeeded the Soviet Union in Central Asia, there is a functioning dictatorship. The dictator has the usual problems of government with a possibility that he will be assassinated or overthrown added on. Presumably the dictator pays more attention to that possibility than to the routine of government. Nevertheless, there have been cases in which the dictator gave good government. Pinochet, after his government was firmly established pioneered in the establishment of an open economy. At the moment he is being followed by many other governments many of which are not dictatorships. Why elected governments such as in, for instance, Argentina to pioneer a dictatorial return to late 19th century economic policies is hard to understand.

It should be remembered that Pinochet established his dictatorship by shedding a good deal of blood. Thus his rule was not an unmitigated boon to his citizens. When he permitted himself to be voted out, his democratic replacements, in general, followed his policies even though they had criticized him fairly strenuously.

But note that Pinochet is an exception. Most dictators do not give particularly good or particularly bad governments. If you ignore their habit of killing people who they suspect are conspiring against them, their government is usually in policy very similar to an elected government. This is not because they favor democracy, but essentially because they do not have very original minds in policy matters. Insofar as they think about the government, preventing themselves from being removed is a very serious preoccupation and they are likely to simply pick up prevailing fads of one sort or another for governmental policies where the throne is not endangered.

In recent years the possibility of the dictator putting money in a Swiss bank has changed this type of government. A Roman ruler like Augustus had no way of keeping his fortune after he retired. Further he could not pass on his money to his heirs although he might be able to pass on the throne. Now it's possible for him to retire as a wealthy citizen of some country other than his own. This has no doubt changed the motives of the dictator, but it's a little difficult to say just exactly how it has changed them.

So much for dictators, which are so common today, but as a matter of fact, have not been very common historically. Some kind of monarchy with a regular way of transmitting the throne is the common form of government over the long sweep of history. Further it is obvious that most dictators would like to pass on the throne to some younger member of their family. Long ago when I wrote a book *Autocracy* (Tullock 1987).

### **Monarchy**

I predicted that the current dictatorships would eventually be replaced by regular monarchies. The process has taken place in three countries, Syria, North Korea, and the Congo. In each of these countries the current ruler is the eldest son of his predecessor. The disturbed situation in the Congo means that particular throne is very unsteady.

Although dictatorships are quite common today, they have not been very common over the long sweep of history. Some types of monarchy with rules for replacing the monarch when he dies are the norm. It should be pointed out however that even a hereditary monarch might be replaced by a coup, assassination, or revolution. Uneasy lies the head that wears the crown. Even a King in a long-established line of hereditary rulers will and should worry about the sword of Damocles suspended above his head.

Normally the rules for replacing the King

transmit the throne to a relative. We Europeans tend to think it should be an eldest son, and that has indeed been frequent in Europe. We inherited the Greek or Roman family system in which a King or other man has only one legal wife. Thus his child by that wife takes priority over other children. The system does not always work out well. When Alexander the Great died, his official heir was his half-brother who was mentally defective. A brief effort was made to install him as the replacement and then the unborn child of Alexander was temporarily crowned by placing the crown on his mother's womb. Both of these failed and the end result was a long series of wars between Alexander's generals.

In many cases in which there is no eldest son a daughter has taken the throne as Queen. Elizabeth will do as an example, indeed as two examples. More commonly some more distant relative is recognized as legitimate heir. Civil wars, however, are no means uncommon in hereditary monarchies. The wars of the roses are a particularly good example of the kind of succession fight, which is apt to occur from time to time in hereditary monarchies. It started when the reigning King became insane and was replaced by a relative. This set off a long and disastrous Civil War in which all of the legitimate heirs were killed. Henry the seventh eventually took the throne after his victory at Bosworth field, but he had no real blood claim on the throne. The previous Plantagenet dynasty was replaced by the Tudor family. The Welch soldier of fortune that was Henry's father was named Tudor and hence the replacement dynasty bore that name.

Although England had a more disturbed succession than was normal on the continent, it was not remarkably out of scope of the usual process to create a new King. The hundred years war between England in

France was set off when the King of France died without a son. The King of England claimed he was heir, although his claim is hard to make out. In any event the outcome of this, the 100 years war, was at least as destructive as the wars of the roses.

But mostly, however, in Europe the candidate for succession was the clear and civil wars occurred only rarely. Before turning to discussing type of government that this led to let me consider other parts the world where King's normally had harems and many sons. All these sons probably wanted to replace their father and in some cases this lead to dangerous civil wars. But there were ways of keeping the matter under control. In China for example the eldest son of the principal wife inherited. Under the Ming, the other sons were provided with a sizable pension and a nice Palace somewhere remote from the national capital. This worked well and the dynasty was replaced by the barbarian Ching without internal civil wars between the sons.

The Ching were, as I said barbarians, and at first had a different method. The Emperor in consultation with the tutors of his sons would choose one as his successor. The system was retained for the first four Emperors' and produced rather above average occupants for the throne. Unfortunately the fourth Emperor adopted Chinese customs and selected the eldest son of his principal wife. This turned out to be a disaster. The new Emperor was one of the worst in the whole history of China. Further his reign happened to coincide with the arrival of the British Navy in force. Whether retention of the more traditional Ching method of getting an heir would have saved the dynasty is not obvious, but at least it could not have done worse.

Civil wars between sons of the last ruler were common, however, in societies where the King had a harem. Selim the grim selected a suitably grim solution. He enacted

a dynastic law that whoever among the Sultan's sons became the new Sultan must execute all the other sons of his father. The sons were kept in a special Palace with eunuchs and females who were thought to be infertile. On the death of the reigning Sultan, there was a small Civil War in that Palace and the successor then did execute all of his brothers and half-brothers. The system did not produce distinguished Sultans, but then, probably, no other system would have done so either.

As I pointed out hereditary monarchy is a commonest form of government in history. To the modern citizen in appears bizarre, this should lead to curiosity as to why it holds such a large role in history. The French monarchists are responsible for a fairly strong argument for hereditary monarchy. Whether it is true or not I will leave to the reader, but it seems to be worth consideration.

Let us began with the monarch himself. The founder of the dynasty was like the dictators discussed above, and indeed perhaps a dictator, a man of above average intelligence, force, deviousness, and probably below average moral principles. His descendants, however, through problems of gene selection in inheritance, would tend to be more of less normal. As among citizens, some would be very bright, some dull, and the majority average. In a way a government by a King resembles government by the median preference voter. The King, like the average voter would have a more or less median intelligence and character.

As a child the potential King would receive a careful education in things which his parents thought would be important for his role. Unfortunately he would also have a thorough education in expensive ways of entertaining himself. As candidate for the throne and as King he would be surrounded by intelligent courtiers who plan to be his advisers. In this he once again is like the

average voter. People who campaign for the average voter's favor, i.e. candidates for office are also more intelligent than the average voter. In both cases there would be other people with well above average intelligence who fill the lower ranks of the government. The voter, like the King, would have a lot of advice some of it good, some of it bad, and would have to select which he followed

The average voter, however, feels it unnecessary to give much attention to the matter. He knows that his vote is only one of among thousands even millions and it is unlikely that improving his opinion of some area will have much effect on the actual policies adopted by the government. For the King this is not so. He would be well advised to think matters over carefully, although he may still make many mistakes. His access to expensive and complicated forms of entertainment may mean that he doesn't think about the matter as carefully as he should. There is also the fact that the average voter when he thinks about the matter aims at benefiting the voters while the King aims at benefiting the King. For reasons to be given below, the question of whether the errors made by the average voter do more harm due to his ignorance than the errors made by the King because his goal is different, is an open one.

So far I have not turned to the heart of the French monarchist argument for hereditary, absolute, monarchs. Putting matter in modern terms they argue that the externality problem does not cause difficulty for the monarchy. Since he owns everything there aren't any real externalities. Government projects cost him money but then he gains the full benefit. Think of the citizen who is considering whether he should pave the driveway to his garage. It will cost money but then he will gain from it. Is the cost or the gain greater? The King deciding to rebuild part of the road

network faces exactly the same question except that both the costs and the gain come to him a little indirectly. The benefit is his benefit, and the cost is his cost.

Although this is undoubtedly an advantage, is by no means obvious that it is a decisive advantage. The situation is rather like that in which a young man inherits a company from his father. Although Ford Motor Company is a gigantic example of this, smaller examples are by no means uncommon. The author of this book is on the Board of Directors of a small company which went through such transition. In most cases and certainly in the case where I am involved the successor does not appear to be as competent as his father. Normally either sells out and retires or is eliminated by the market. Occasionally he turns out the competent and keeps control. The King does not face the market tests which tend to eliminate the hereditary President of a small corporation so quite incompetent Kings may continue to hold power. George III wasn't sane during the latter part of his reign, but nevertheless passed on a, much diminished, throne to his legal successor.

Nevertheless the system is a commonest form found in history. The fact that most of my readers are pretty much unfamiliar with it, although they no doubt think that it is wrong, means that a few paragraphs discussing it is worthwhile. It is frequently criticized essentially on several grounds, a commonest of which is simply that it is not a democracy. That is, of course, true, but in view of its frequency in history seems somewhat inadequate.

Monarch these are frequently criticized on the grounds that they are extravagant in providing facilities for the monarch. Certainly anyone who visits Versailles, or better yet the Imperial Palace complex in Peking, which makes Versailles look like a mud hut, is impressed with the funds spent for the Royal

dwelling. It is not obvious, however, that the share of GNP taken by the Royal dwellings is greater than that taken by the president and Congress for their income and direct expenditure on people hired primarily to help them get reelected. In any event the total is a small part of the national income. It may well be a waste, would not really a big waste.

It should be kept in mind that both of these Royal residences were also office buildings for much of the government. If you subtract the office part of Versailles, the remainder is probably not much more than twice the size of some of the Chateau on the Loire. Most rulers are not very imaginative and whether their house has become the largest one in the Kingdom, they may be unable to think of any expansion, which would be to their advantage.

This of course is dealing with large countries like China or France. The many petty rulers who ruled Germany or Italy before unification probably plan their houses not to compete with their subjects, but with the next ruler over. Thus although their palaces are small compared to Versailles, they may have absorbed considerably more of the national income of, let us say, Wurtemberg than Versailles did of France. Nevertheless, most modern students would regard this as wasteful even if not a gigantic waste. But it continues with constitutional monarchs. The Palace of the Queen of England or the King of Sweden are very extensive and could be regarded as wasteful although it is clear their citizens do not begrudge the funds.

A second criticism with regard to the European monarchs was that they fought unnecessary wars. It is sometimes said that war was a hobby of King's. Granted the fact that the biggest and most expensive wars of European history were either the collection of wars set off by the French Revolution or the two world wars of the 20th century, this

criticism is dubious. The United States managed to have its largest war, in terms of share of GNP absorbed, entirely domestically. The First World War was fought between countries, which either were democracies or rapidly becoming democracies. In the Second World War democracies certainly played a major role.

It would be foolish to allege that the monarchies were peaceful, but compared with the democracies that succeeded them or the classical democracies of Athens and Rome, alleging that they were particularly warlike seems unlikely.

There is an intermediate form of government between absolute monarchy and democracy. In this case the King is not completely sovereign because there is a collective body of some sort, which he must consult. In feudal times the Army of the Kingdom was essentially the higher nobles and their personal retainers. Under the circumstances the King could hardly take action, which they vigorously objected to. Consulting them from time to time was wise; hence, the House of Lords and its duplicates in many kingdoms on the continent of Europe. Louis XIV abolished his and when his successor Louis XVI tried to revive it he lost his head.

## **Republics**

In England, Simon Montfort, Earl of Leicester led a revolt against the King and as part of his revolt summoned each local government in England to consult with him. When the King won and beheaded the great Earl he decided to keep the body in existence and hence the House of Commons. It should be emphasized that this was not very democratic in the days of the rotten boroughs. Only a few of the seats were settled by elections involving a significant number of voters. Old Sarum was a plowed field sending two MPs to London. One of the MPs sitting for old Sarum was



prime minister during much of wars with French republic and Empire. Since he was successful in seems that this particular way of getting representatives worked out well at least occasionally. It should be said, parenthetically, that the Pitt family held in fee simple six seats in Parliament.

The system which began to be replaced by more democratic approach in the mid-19th century, presided over not only the defeat of the French republic and Empire, but also the beginning of the industrial revolution. Judging by results it was clearly a very successful government although whether that is simply a statement that random behavior sometimes works out well or a statement that it was a good form of government, I will leave to the reader.

There is an intermediate form of government in which a minority makes up the voting public, but they actually do vote. The Venetian republic will do as an example. A hereditary body of about 5 percent of the adult males actually in residence in Venice elected the Doge and other higher officials of the government.

It is notable that the voting body of the citizens seemed to take an active role in the actual government. Those gigantic halls in the Ducal Palace were where they met and large numbers of them seem to a turned up quite regularly to transact the business of the government. Since many of them were active merchants this is quite remarkable. It may be that the active participation of the eligible voters was one of the reasons the government ran reasonably well.

The achievements of the Venetian republic were immense. A sandbar was converted into one of the world's major beauty spots. Their cultural achievements during the Renaissance were remarkable. They pioneered in printing. In science, Galileo was a professor in the Venetian University when he did his most important work. His departure from Venice is

strongly reminiscent of what happens when a leading member of the faculty of one of our universities gets a better offer from elsewhere. If he had stayed in Venice they would have protected him from the inquisition, but he could hardly predict that he would have that particular cost imposed on him in his new post. Vesalius was also a professor in their University.

In addition to the cultural achievements, Venice was a significant military and imperial power. They held much of the Po basin and a good deal of real estate in the eastern Mediterranean. For a considerable time their navy was the principal protection of Europe against Turkish naval power. Their eventual conquest by Napoleon does not indicate military or political feebleness. Many larger countries were conquered either by the French Republic or by Napoleon.

The actual structure of the government and the election of the higher officials was carried out in a way which insured fairness, but was intended to prevent the kind of interfamily quarrels which destroyed most of the Republics in Italy. It does not seem likely that any new government will adopt their methods but for the curious reader I described them in the appendix of my *On Voting* (Tullock 1998).<sup>ii</sup>

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